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TRADE AND COMPETITIVENESS ISSUES

HEARINGS

BEFORE THE

COMMITTEE ON SMALL BUSINESS
HOUSE OF REPRESENTATIVES

ONE HUNDREDTH CONGRESS

FIRST SESSION

WASHINGTON, DC, MARCH 18, 19, 24, AND 25, 1987

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TRADE AND COMPETITIVENESS ISSUES

WEDNESDAY, MARCH 18, 1987

House of Representatives,
Committee on Small Business,
Washington, DC.

The committee met, pursuant to notice, at 1:10 p.m., in room 2359-A, Rayburn House Office Building, Hon. John J. LaFalce (chairman of the committee) presiding.

Present: Chairman LaFalce; Representatives Mazzoli, Olin, Hayes, Bilbray, Mfume, Flake, Lancaster, Campbell, DeFazio, McDade, Slaughter, Meyers, Gallo, and Upton.

Chairman LaFalce. The Small Business Committee will come to order. Today's hearing is the first in a series of hearings which the Committee on Small Business will hold on the competitive problems and opportunities confronting the United States small and mid-size companies in the new international economic environment. These hearings are preparatory to committee consideration of a small business title to the House omnibus trade bill the first week of April. Through the hearing process, the committee will explore the proper role for Government policy in enhancing the competitive prospects of U.S. companies.

Up to this point, there has been a serious gap in the trade debate, an important section of the economy whose problems have been virtually ignored. Our small and mid-size companies are key sources of economic growth and adjustment. Yet their unique concerns have remained largely unaddressed. I am, therefore, very pleased that the House leadership has asked the Small Business Committee to give attention and focus to these important concerns in the trade bill.

Small and mid-size companies account for half of our private work force, produce half of our gross domestic product, and have created nearly two-thirds of the new jobs of the last decade. These companies are the driving forces behind many of our advances in technology. Three-quarters of America's great corporations rely on small firms as suppliers, manufacturers, distributors, and customers. Entrepreneurs have spawned new businesses, indeed whole industries, while bigger firms have all too often been mired in outdated business practices. The success of many of our mid-size growth companies establishes that U.S. industries—whether manufacturing, services, or high tech—can meet the challenge of international competition.

But the potential of small and mid-size companies to continue to contribute to the growth of the American economy and the overall international competitiveness of the United States is increasingly at risk. Smaller manufacturing firms are disappearing as U.S. multinationals rely increasingly on a foreign subcontractor base. Difficulties in acquiring and applying new technologies inhibit growth and revitalization, and capital formation is inadequate. Few mechanisms foster investment in smaller firms and these firms are largely ignored by the institutions that dominate banking and finance.

Public policy has done little to help. The Commerce Department laments the fact that 20,000 to 30,000 smaller U.S. firms have unrealized potential as exporters, while those firms which do try to export face bewildering bureaucracies and byzantine regulations.

Too many dichotomies have dominated the trade debate—labor versus management, government versus business, large companies versus smaller firms, Congress versus the Administration, Democrats versus Republicans. We can no longer afford the luxury of quibbling among ourselves as our competitive position deteriorates. Government, business, and labor must work together to develop competitive strategies to put U.S. companies at the forefront in international markets and create the environment which will allow those strategies to work.

In the business world itself, competitiveness is a two-way street. We must develop a competitiveness strategy that integrates the needs and strengths of smaller and larger firms. Larger corporations rely on their subcontractor base for the product quality and innovation that can put them at the forefront in international markets. Smaller firms look to the larger multinationals for the marketing experience and distribution networks that can move them into the global marketplace. Most importantly perhaps, the emphasis on quality, value, innovation, and service that is typical of our best small and mid-size companies can help to shift the corporate ethic that would place more emphasis on short-term gain than long-term competitive strength.

In much of the trade bill, we are working largely to prevent further erosion of our trade position. Lacking a strategic response, we have watched our great manufacturing enterprises and many high technology and service firms falter. Irreparable damage has been done, and we are working largely to prevent further erosion.

But it is also time now to look forward and take positive steps to provide the environment in which U.S. companies can flourish; to rethink the potential of entrepreneurs and small and mid-size companies as forces for economic growth; and to help provide the competitive environment in which that growth can occur.

We must make competitiveness the linchpin of our economic policy. To do so, we must expand export opportunities; minimize impediments to the growth of smaller innovative firms; facilitate technology transfer; increase access to long-term capital; and generally create the conditions that foster innovation and business development. Innovation, the engine of economic growth in the modern world, can prosper only in an environment that encourages new ideas, even at the expense of the old.

We are fortunate to have as our opening witnesses for this particular series of hearings: Milton Stewart, president of the Small Business High Technology Institute; William Lilley III, president of the American Business Conference; Fred Bergsten, director of the Institute for International Economics; James Harvey, executive director of the National Commission on Jobs and Small Business; Roger Little, co-chairman of the National Innovation Network and president of the Spire Corporation; and Gordon Johnson, president of Johnson Associates.

TESTIMONY OF MILTON D. STEWART, PRESIDENT, SMALL BUSINESS HIGH TECHNOLOGY INSTITUTE

Mr. STEWART. Thank you, Mr. Chairman. I am going to content myself, if it meets your pleasure, with first congratulating you on assuming the Chair of this committee. It has been my good fortune to appear before it and work with it for many years. We are very hopeful that the 100th Congress will come to grips with several major remaining issues.

We hope in brief that this particular proceeding will address and begin the resolution of some of the most perplexing problems that we have, the relationship between our own small business community, and world trade.

World trade and taxes are probably the two areas, as I look back over the years, in which we have more left undone than any other, and they are a handful.

I tried in my own statement to briefly highlight what I think is the most pressing problem we have in our own country and that is the disastrous erosion of our technology base. That is why the SBIR program's improvement must have such a high priority.

The two general recommendations that I have made have been endorsed by the National Commission on Jobs and Small Business. One of the two was recommended by the White House Conference on Small Business. I have included as appendices material referring to them.

First, I believe that we still need in foreign trade—and this day can start it—the kind of turn-around in the national thinking about small business which grew out of the 1980 White House Conference on Small Business.

I have suggested that the best way to launch that kind of turnaround is through a conference of international small business people under the aegis of the summit nations.

Second, I have suggested that this committee and the Federal Government more aggressively draw the States into a Federal/State program, a new one. I have not tried to describe it. But I have said in passing that it has seemed to me that the Federal Government has been giving signals reflecting overload for some years now.

And now it appears to me that it should concentrate on a program in which administration and management were left to the States, and funding perhaps was done jointly. I may be wrong about this. We all have different experiences, but that is the impression that I have.

I think, Mr. Chairman, that I will content myself with those remarks, and leave the rest of it to two colleagues of mine from the small business community who are far more competent at the specifics of foreign trade than I can possibly be—Roger Little and Gordon Johnson.

Their backgrounds are described here. They both have had long years of personal experience in managing growing small companies, competing with foreign firms in the United States, exporting and competing in foreign markets.

I want to close simply by thanking you again. I will be happy to enlarge on my statement, which I ask to be included in the record at this point, and I will be happy to answer any questions that anybody has.

[Mr. Stewart's prepared statement, with attachments, may be found in the appendix.]

Chairman LaFalce. Thank you very much, Mr. Stewart. What we are going to do now is proceed in the order that I suggested initially, and call upon Mr. Lilley, the president of the American Business Conference.

TESTIMONY OF WILLIAM LILLEY III, PRESIDENT, AMERICAN BUSINESS CONFERENCE [ABC]

Mr. Lilley. Thank you, Mr. Chairman, and thank you for inviting the American Business Conference to appear. I, too, want to congratulate you on holding these hearings. With all of the focus on the trade issue on Capitol Hill, I am glad that someone finally is focusing on exports as well as the import problem, and also on business clusters that are other than large scale. I believe that both emphases deserve attention.

Let me say a word first about the American Business Conference. It is made up of 100 chief executive officers of mid-size companies. And the definition for mid-size is revenues between $25 million and $2 billion. The average revenues last year for an ABC company was about $380 million.

Those revenues grow on average per year about 35 percent, and they create jobs for their companies at about 14 percent per year. The companies in the American Business Conference are spread evenly across manufacturing, high technology manufacturing, and the various service sectors. So it is a good spread for the American economy.

It is a bit of an unusual Washington organization in that you have to achieve something other than the ability to pay dues to get in. You have to grow at a rate of 15 percent per year. And if you do not achieve that, you are asked to leave.

About 20 companies fail out each year, and they are replaced by other companies.

In anticipation of an event like today, we began an extensive survey of our members last fall on the whole issue of international competitiveness. And along with McKinsey & Company, we asked them four questions.

We asked their CEO's how important international competitiveness was to them and to this country. We asked them how they were doing internationally. We asked them what problems they were having internationally, and we asked them what they wanted the Federal Government to do about those problems.

Each of you has a copy of our study in front of you. It is the gray report entitled "The Challenge of Global Competitiveness." I note, among other things, appendix 1 which is the survey questions.

More important, appendix 2 is the fold-out of the companies. Many of you enjoy having companies in the districts that are represented here.

On the question of how well these companies are doing, our results yielded very unusual and perhaps controversial results. These companies are doing very, very well abroad. From 1980 to 1985, their internationally derived revenues grew 230 percent, roughly an annual average of 27 percent per year. They project the same rate of growth for the next 5 years.

So fast have their international revenues grown that where in 1982 only 13 percent of these companies' revenues were internationally derived, last year 22 percent were internationally derived.

We asked these CEO's how did they account for this success, particularly this extraordinary rate of success across incredibly varied lines of businesses, and the answers were uniform. They said primarily they relied upon managerial skill and managerial will. And they said that reflected itself in two qualities, product quality and marketing quality.

They linked around that a host of nouns—aggressiveness, agility, risk taking, patience, and willingness to take losses. Those are all reflected, if you would open the little booklet, on the chart on page 10.

In a very unusual exercise, we asked them to grade themselves against the foreign companies with which they compete. You will notice that on all of the types of business measurements which measure quality that the American companies out performed the foreign companies. But on all of the indicia that are cost based, the non-American companies were lower cost performers.

Now that point goes to what they regard as the fragility of their success. Because they are not the low cost producer, therefore to continue penetrating international markets as rapidly as they are, that control of costs is imperative.

How they control their costs is different than most companies or at least different from the standard dialogue on the Hill. In the first place, these 100 companies are all high wage companies. The lowest wage company very successful abroad is probably Dunkin Donuts, which we would classify still as a high wage company.

The companies say that control of labor costs is not a very relevant factor either in terms of international competition or domestic competition. They rank their costs on page 17. And you will see that labor costs and resource or material costs are now the lowest costs that they have. The higher costs are market access, number one; second, the cost of capital and taxes; and then third, market support.

What you have in these companies, if you think of the companies of the 1960's and the early 1970's which made us dominant worldwide, these newer companies have reversed the cost pyramid. And compared to the kinds of costs of the labor intensive and volume intensive companies of the 1970's, these are the opposite. These companies are quality added, capital intensive, knowledge intensive, and technology intensive.

These kinds of companies are probably the companies, at least they appear to be, that are going to carry this economy forward both domestically and internationally.

The second problem that they had related to barriers abroad. Again we turned up very, very controversial findings. They said that by far the biggest barrier to penetrating international markets was the cultural preference or cultural bias most sharp in Common Market countries and Japan that American made goods were of inferior quality to the goods, this a perception whether true or not, a perception, are of inferior quality to the goods made in the Common Market or Japan. Finally, on page 18, we list the Government barriers that these companies face.

Last, when we asked them what they wanted you to do to facilitate their success and the success of other companies small and mid-size like theirs, they had two things that they said were most important.

And the first is that the Government avoid any kind of actions that would trigger first protectionism, and then a retaliatory cycle based on that protectionism. They believe, because they are so successful abroad because of their exports, that if a retaliatory cycle begins that it will be their companies and their products which will be taken hostage.

The second thing that they want the Federal Government to do is reduce the domestic deficit. The size of the domestic deficit is eating the savings in the country. Relatively speaking, it is making their cost of capital more expensive than the companies that they compete with from West Germany or Japan.

Middle range in importance that they would like the Federal Government to do is to streamline and reduce the burden of the export licensing program.

And finally, last on their list, are two things: They would like the Federal Government to recognize that the problem that we face today as a country in terms of exports, that problem has been a long time coming. It relates to the educational system, labor/management relations, the way that our financial markets are structured for quarterly pressures, and a whole host of things that were 15 years in the making and are not going to be fixed by one Congress in 2 years.

The last thing that they would like is that the Government in working against other barriers in other countries that the Government moves in an agile fashion using a scalpel rather than a shotgun. ABC companies want barriers knocked down in a way that avoids protectionism and subsequent retalization. Thank you.

[Mr. Lilley's prepared statement may be found in the appendix.]

Chairman LAFALCE. Our next witness will be Mr. Fred Bergsten, director of the Institute for International Economics. Mr. Bergsten.

TESTIMONY OF C. FRED BERGSTEN, DIRECTOR, INSTITUTE FOR INTERNATIONAL ECONOMICS

Mr. BERGSTEN. Thank you very much, Mr. Chairman. You launched the session this afternoon by saying that you wanted to focus on opportunities and problems, and I am going to talk a bit more about opportunities for small business given the overall outlook, as I see it, for the imperatives facing the American economy over the next few years primarily in the international area.

My conclusion is that the American economy is going to have to achieve export led growth over the next 5 years. That will come as a stunning surprise to many Americans, since we have never thought of our economy as being led by export expansion.

We have thought of Japan, Korea, Europeans and others as having focused on the international sector. But I am going to briefly explain why I think we have to orient our whole economy in that direction, and the implications that may have for small and medium sized businesses.

Chairman LAFALCE. And if your thesis is true, that is an awfully strong argument again against protectionism.

Mr. BERGSTEN. Exactly. Just to underline what Mr. Lilley said, I think that this would be the worst conceivable time for the United States to move in a protectionist trade direction. We have gone a long way now to restore our competitive position in world trade. And we are now poised, if we do the right things, to exploit that opportunity to achieve export led growth.

But if we went protectionist just at this time, when other countries on my prediction are going to be facing very deep internal pressures to go protectionist, we would be undercutting all of the opportunities that we face.

I have three strands to my argument. The first is to simply look at America's own international position. Last year, we ran a trade deficit of about $150 billion, but that is only the start of the problem.

Over the last few years, we have shifted from being the largest creditor country in the world to being the largest debtor country in the world, because we had to borrow so much to finance these massive trade deficits. So in the next 3 or 4 years, we will be paying $25 or $30 billion of interest net to the rest of the world. That will be a foreign payment that we will be making on top of the $150 billion trade deficit.

In addition, and it is highlighted by some stories in the press today, our oil import bill is probably going to start rising again. Our dependence on foreign oil and the volume of our oil imports will undoubtedly be rising over the next few years. We hope that the price does not go up much, but it may go up again. In any event, the oil import bill is going to rise.

So when you put those three things together—the enormous trade deficit that we now face, the increase in interest payments to foreigners on our international debt which is growing so rapidly, and an almost certain increase in our oil import bill—what you find is that the United States is going to have to improve its trade balance by something like $200 billion in order to get back even to balance in our international accounts.

I say "even" to balance, because traditionally the United States was a surplus country running a surplus in our current account. There are many people who think that it would be appropriate for us to go back into surplus. If we did that, we would have to achieve an even greater turn-around from where we are today.

But just to be on the conservative and modest side, I will suggest that our proximate target ought to be a gain of about $200 billion. And that obviously is going to require a lot of export led growth.

The second point, even leaving aside our international position, is that export led growth is going to be essential for the overall health of our economy as a whole.

If you look at all of the forecasts for the American economy over the next couple of years, 1987 and 1988, they come in with fairly modest expectations—2, 2.5, or 3 percent depending on the forecaster—but all of those forecasts get up to even a 2- or 3-percent growth level only with a significant improvement in our trade balance contributing at least 1 percent a year to our total economic growth.

The point is that if our trade balance did not improve, we would have a growth recession at best—meaning growth in the 1- to 1.5-percent range with unemployment rising again—and we would have a real recession at worst.

So on almost any forecast that you can look at, the outlook for the expansion of the overall economy is simply dependent on the trade balance improving.

The third point, and it is related, is to suggest that over the next few years American industry will probably not have the same buoyant growth in domestic consumption that it has had over the past few years.

One reason simply is that we need to make room in terms of output going abroad to get the export expansion, and have the goods sold abroad rather than sold at home. But, also, the underlying forces that have compelled consumer demand rapidly upward over the last few years are tending to peter out.

Growth of real incomes is modest. The savings rate has dropped to an abnormally low level, and it is undoubtedly going to bounce back—meaning that the consumption share of income will drop. All of those forces mean that our industry, including small business, is unlikely to face the kind of growth in domestic consumption that has enabled it to keep going reasonably well these last 5 years, and will have to look abroad for markets.

And, so, for three basic reasons, it seems to me that export expansion has to be a focal point of our total economic strategy over the next 3 to 5 years.

Now that obviously raises the question: Can it be done? If we are facing this massive trade deficit, is it even feasible to talk about a turn-around of this kind of magnitude?

My answer is a qualified yes. The reason that I say yes is both because of the success of companies, as Mr. Lilley has referred to and I will come back to in a minute, and because the decline of the exchange rate of the dollar over the last couple of years does in fact restore a good deal of our international price competitiveness.

In my view, it was the rise of the dollar, by about 70 percent against an average of the other major currencies from mid-1980 to early 1985, which was responsible for about three-quarters or so, of that trade deficit that we ran over the last few years. I put most of the weight on the exchange rate of the dollar, and the budget deficit and macroeconomic forces that underlay it.

But the fact that the dollar has now come down by 35 to 40 percent against the other major currencies does in my view offer us a significant opportunity to get back into world markets in a meaningful way.

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Now the reason that this is a qualified yes is because additional steps, obviously, are needed to fully restore our export competitiveness. Economic growth in some of our major markets, particularly Europe and Japan, is very sluggish and needs to be stimulated to provide markets for our trade to improve.

The currencies of some countries, notably Taiwan and Korea to a smaller extent, have been rising a bit against the dollar but need to go up further to enable us to regain price competitiveness there. And the dollar may need to fall a bit further against the yen and the European currencies as well.

But I would submit that American firms can compete again and should lose no time attempting to do so. Now I also take some comfort, and here I might disagree a bit with what Mr. Lilley said, from the fact that if you go back and look at the period just before the soaring rise of the dollar priced us out of world markets, U.S. trade performance was actually very strong.

If you look at the period 1978 to 1980, American exports were growing twice as fast as world trade. We regained global market share in every single sector of industry and in every single geographical market in the world, in some cases back to the level of the 1960's.

In just the 2-year period 1978 to 1980, our current account balance, our balance in goods and services, improved by $60 billion excluding the direct adverse effect of the second oil shock. And even when you put that in, we moved into current account surplus as recently as 1980–81.

So, to those who say that America cannot compete and is a hopeless case, I say the facts do not support it. We have priced ourselves out of world markets. We let ourselves become uncompetitive to a very crucial extent. But I think that the underlying position based on the most recent history is quite promising.

Now by that I do not mean to say that we should not do everything possible to deal with the underlying issues that Mr. Lilley mentioned; the educational system, support for R&D, investments incentives, and the like. We clearly should do everything that we can in those areas to maximize our competitive strength, but I think that the underlying record is in fact encouraging and therefore is an opportunity for American industry and small business.

Finally, what in the way of specific suggestions, other than the ones that I have already mentioned: Further movements in the exchange rate, growth abroad, and obviously reducing our own budget deficit as part of that picture.

I think that a renewed American export boom on anything like the scale that I suggested, and which is possible, will just not happen on its own. There will have to be a major marketing push by American industry to recapture markets abroad, especially in today's world where competition is so keen among countries because growth is modest and inflation no longer hides industrial flaws.

Such a marketing push, I would suggest, is particularly necessary because many American firms simply became demoralized trying to export during the first half of the 1980's when the dollar priced us out of world markets and their positions deteriorated so badly.

Many firms simply withdrew from export markets and stopped trying to exploit international opportunities. Those firms, which include some of our largest as well as many smaller firms, face a reentry problem in the world markets of substantial magnitude. They are going to have to redistribute resources to selling abroad and make important corporate decisions to do so.

It seems to me that that problem may be especially acute for small business in the United States. The vast bulk of our exports have always come from a handful of mainly large companies.

The Commerce Department estimates that in 1984, the latest year for which data is available, that only about 2,300 companies accounted for over 85 percent of our total exports. About 2 percent of the total firms of the country accounted for 85 percent of the exports suggesting that there is a wide universe of companies out there that are not even involved in international trade but which will have to do so to achieve anything like the results that I mentioned.

In general, most small business has not been oriented abroad, but will have to do so if we are to achieve the national economic goals that I mentioned.

Most of the leadership in marketing and reentry will have to come from the private sector itself. But the Government has got to do what it can to help, and should in fact make every effort to encourage a renewed export push by American industry, especially that part of industry like small business which has not heretofore been very active.

The most promising Government instrument for playing such a role is probably the Export-Import Bank. The Export-Import Bank can both finance export efforts by American firms and make its expertise on foreign markets available to them, thus sharply enhancing their prospects for selling abroad.

Through its small business program, Exim should be particularly helpful to the companies that are of concern to this committee. To carry out such a mandate, I think that the omnibus trade legislation that you are now considering should sharply expand the resources and the mandate of the Export-Import Bank.

Its direct lending and guarantee authority should be increased considerably. It should be directed to use those resources aggressively to expand markets for our American exports including by matching subsidy practices of foreign export credit agencies wherever those exist.

I think that you ought to reexamine the accounting treatment of the Export-Import Bank, so that only its real costs to the taxpayer—which is any subsidy element in its programs—is counted as a budget outlay.

I submit that the Export-Import Bank, working with the Department of Commerce, should lead the market reentry effort of American exporters. I believe that would be of particular help to small business where I think that enormous opportunities lay in the international field and are indeed essential if the country is to achieve anything like a satisfactory outcome for the major outcomes that I cited at the outset over the next 5 years. Thank you very much.

[Mr. Bergsten's prepared statement may be found in the appendix.]

Chairman LAFALCE. Thank you very much, Mr. Bergsten. Our next witness will be Mr. James Harvey, the executive director of the National Commission on Jobs and Small Business.

TESTIMONY OF JAMES J. HARVEY, EXECUTIVE DIRECTOR, NATIONAL COMMISSION ON JOBS AND SMALL BUSINESS

Mr. HARVEY. Thank you very much, Mr. Chairman. Mr. Chairman, you are likely to be overwhelmed with the congratulations you are receiving as you assume the chairmanship of this important committee, but I would like to add my best wishes. And I would also like to thank you and to congratulate you and the ranking minority member of this committee, Mr. McDade, for your leadership in seeing to it that the National Commission on Jobs and Small Business was established nearly 2½ years ago.

I am here to discuss the report of the Commission, "Making America Work Again: Jobs, Small Business, and the International Challenge."

By way of introduction, Mr. Chairman, I would like to note that the Commission was created in September 1985 upon the request of yourself, the ranking minority member, and 16 other Members of the House and the Senate. It was asked to report back to the 100th Congress with a report on how to create 10 million jobs through small business. "Making America Work Again" is the result of the Commission's efforts.

No Federal funds were involved in supporting this Commission. It was a blue ribbon group representing leaders from all walks of American life, our universities, our small businesses, our great corporations, and our great banking institutions. Former Presidents Carter and Ford graced the Commission as honorary cochairs.

It was financed largely by the Charles Stewart Mott Foundation of Flint, MI, with supplementary support from the Rockefeller Foundation, the Carnegie Foundation of New York, the Mellon Foundation, and also from the MacArthur Foundation.

I can be fairly brief, Mr. Chairman. I think that many of the themes that are in this report have already been discussed by the witnesses who preceded me. I do want to say that something remarkable is probably going on in this country.

On February 4, we presented this report to the 100th Congress. On February 5, the American Business Conference came out with another excellent report, "The Challenge of Global Competitiveness."

So these two groups, representing small firms and representing small and medium sized firms, both unknown to each other were working along the same track. And I think that there is some mood in the country, some tide moving here, that the 100th Congress can grasp.

Let me talk very briefly about the three themes in the Commission's report, and then touch on the five major areas of recommendations that the Commission worried about.

The first theme is international competition. As "Making America Work Again" makes clear, we are now living in a new age and a different world in which the United States has become in the words of the report, "an import sponge." Our inability to compete in world markets has created major difficulties for the entire economy.

We are now the largest debtor nation in history. Trade deficits have mushroomed in the 1980's. But they have been going on not simply since 1980—since 1971, the United States has showed a trade surplus in only 2 years.

Unemployment remains far too high. We would not have accepted the unemployment rates that we currently have when I first came to this country in 1960. When I first came here, unemployment of 4.5 percent or 5 percent was considered way too high. Now we seem to be quite happy with 6.7, 6.9, and 7 percent unemployment rates—rates that are way too high by traditional American standards.

We are losing world market shares across the board. Since the early 1970's, the United States has lost about one-third of its world market shares in manufacturing, in textiles, in electronics, engines and turbines, and even in the areas of America's traditionally greatest strengths, agriculture and high technology.

The second theme is an outgrowth of the first. Our economy's capacity to support its people is in some jeopardy—the ability of the American economy to continue to provide productive employment for large numbers of its citizens is increasingly in question.

The evidence that the Commission puts forward in this report I think is disquieting to serious men and women. Since 1980, we have lost over 1 million manufacturing jobs paying $25,000 a year or more, and we have replaced them with 5.5 million jobs in service and retail industries paying half that amount and less—paying between $5 and $7 an hour.

Real wages and salaries in the United States have been stagnant since 1971 and 1972. And in some cases, they have declined. Average unemployment has increased by roughly 2 percent in each of the last three decades, and that trend shows no diminishment.

The third theme of this report is the theme that brings this committee together today. The theme is that small business is an incredible asset to the United States, and that it has largely, until now, been overlooked.

Small firms, as you said in your opening statement, Mr. Chairman, account for about half of the private non-farm employment in America. They produce 50 percent of the Nation's gross domestic product. They are prodigious generators of new jobs, of new products, innovations, and services. And their capacity to turn on a dime to identify and service new markets is something that we just have to have in the dynamic fast changing economy that faces us today.

I will skip over what all of this means, because the Commission tried to talk about what these developments meant in terms of a real threat to the American dream. I will just content myself by saying that, as an immigrant, I can tell all of you that the American dream is real. It worked for Jim Harvey; it worked for every member of the Harvey family; and it has worked for generations of immigrants in this country.

If we lose that, we lose something that is quintessentially American, and that it is extremely important to people overseas as they look at this country.

The Commission made five recommendations to turn this situation around. I am not entirely sanguine that simply changing the exchange rate of the dollar is enough. Undoubtedly it helps, but we still need to do a great many things to make the United States competitive in world markets.

Let me touch briefly on the five. The first was mobilize our people. I think that the hearing we are having here today is an example of the type of thing that the Commission was talking about.

Recommendation A of the Commission called for leadership on the part of the public and private sectors across the board to mobilize the American people to understand what is going on in the world economy, and it gave specific directions and recommendations for the President, to Congress, to Governors, to mayors, and city council members about what they might do.

The second recommendation was prepare our work force. The report recommended improved educational efforts across the board to help provide workers and managers with the skills that they need to compete in the new world economy, and to help our work force develop the flexibility that it needs in order to adapt to the changing work place.

The next two areas of the Commission's recommendations I know are a particular focus of these hearings. One has to do with business investment, and the other has to do with trade. I would just like to touch on them here, and come back and mention them in more detail a little later.

The first is invest in our future. The Commission recommended doubling business investment in plant, equipment, and technology, and developing new streams of capital for small business.

The fourth area, recommendation D, restore the Yankee trader tradition. The report urged continuing the U.S. policy for the support of fair trade or goods and services and the restoration of a vigorous exporting base that includes a very large number of small firms.

And finally, we went through the normal list of suspects that groups of this sort are inclined to examine when casting around for things that need to be improved. It has recommendation E, clear the decks, a series of recommendations aimed at Government, business, and labor to get their act together to make America more competitive.

It is such things as the establishment of a Department of Trade, balancing the budget, and management/labor relations conference at the White House.

Now let me get back to recommendations D and E, because I think in many ways that they are at the heart of the report. The Commission's recommendations in this area were not developed in a vacuum. We held one hearing on capital for small business at the very site where George Washington was inaugurated on Wall Street nearly 200 years ago.

This is what we heard there. Venture capital is available only for the cream of the crop of entrepreneurial firms in the United

States. Long-term financing for small business in America, that is funds for 5 years or longer is by and large very hard to get hold of.

The dynamics of the financial community amount to almost an institutional prejudice against investment in small business. That is a pretty strong term. But the dynamics include difficulties in administering loan portfolios with very large numbers of small loans, misunderstanding the small business community, prohibitions against financial institutions holding equity positions in businesses, and the lack of a well-developed secondary market to warehouse, market, and recycle small business loans.

As the report makes clear, these problems are particularly acute in low income and minority communities which lack the personal and community savings that are essential to any small business.

We go into a raft of recommendations that you will find in here under recommendation C—balancing the Federal budget, encouraging increased savings in the United States, reestablishing the investment tax credit, creating small business mutual funds as well as the secondary market for small business paper. And the encouragement of long-term capital investment particularly in small business firms through favorable treatment of capital gains.

Restore the Yankee trader tradition. Only 10 percent of American firms export, we learned at our hearing at the Carter Center in Atlanta. And it was not 2,000 companies accounting for over 85 percent of American exports, but more like 250 companies account for about 85 percent of the dollar value of American exports. Huge companies such as Boeing that have these billion dollar contracts overseas. We took that figure from the President's Commission on Industrial Competitiveness which issued its report in 1985.

There are about 30,000 small firms that could export, but they never go near export markets, in part because national and State efforts to identify and service these small firms that have exportable goods are, according to the evidence that we received, notably deficient.

Only 1 percent of SBA loans in the last 4 or 5 years have been used to support exporting. We understand that Eximbank which is required to spend about 10 percent of its foreign sales moneys on small businesses, is not meeting the full authorization requested by the Congress. And we think that something should be done about that.

Clearly we should do better and we have to do better. Each $1 billion that we sell abroad, that we export abroad, supports about 25,000 American jobs.

The Commission made seven recommendations under the rubric of restore the Yankee trader tradition. You can read them, and I will just touch on them briefly. One was expand the general agreement on tariffs and trade to include intellectual property rights and services that are not now covered.

The second was to look into our own import quotas with a view towards removing those that are no longer necessary. The third was expand the exporting base by improving and simplifying the extraordinarily complex provisions of foreign sale corporations which are administered in the Department of Treasury.

One witness said to us that nobody understands FSC's including the IRS. The legal and accounting requirements for establishing a foreign sales corporation are just beyond the ken of most small firms.

The Commission recommended aggressive efforts by the International Trade Administration to work with States and small business groups to disseminate information about programs available to small firms. And in particular, to help small business and to help financial intermediaries to set up export trading companies.

It is very clear—it is clear to me in any event, and I do not want to speak for the Commissioners—that a large part of the success of other nations in exporting and serving world markets is that they made a very serious commitment to export trading companies. I suppose that if someone is trained in history, it goes back to the creation of the East India Company in England in the 18th century.

Government, financial institutions, and business have got to get together to aggressively market their products abroad. The Pacific Rim countries are doing this now. I think that the United States needs to do that in a serious way.

We also had recommendations with respect to marketing data. Recommendations directed at States for leadership in this area including States creating State sponsored foreign sales corporations. And as Mr. Stewart mentioned, a summit nation conference on small business to let small business in the United States learn from small businesses overseas, and to let small businesses overseas learn something about the American small business community.

I have rattled on much too long, Mr. Chairman. The report has a lot to say. I am eager to get it into the record. I hope that you have time to look at it.

If I could conclude, I would say that the Commission did not look at the world through rose colored glasses. Although confident of our capacity to turn the situation around if we take our difficulties seriously, the Commission believed that unless this Nation attends to the changed conditions of enterprise in the world, there are going to be long-term consequences for the United States that will be quite severe.

And the way that the Commission tried to grab the attention of the public to this issue is by saying that it is time that America came to its senses. Because each generation of Americans has exceeded the standards of its parents in income, education, health, and material well-being, we have long taken our prosperity for granted.

But now a new prospect emerges. For the first time in our history, our children's standard of living may not equal our own.

And if that will not get us all working along these lines of an export led resurgence of the American economy, I am not sure what we need to do in order to do that.

I would like to thank you, Mr. Chairman, for the privilege of being able to testify before this committee. I again would like to thank you and Mr. McDade for your leadership in this effort, and to thank you for providing this forum so we can discuss these issues, and hopefully get some action on them.

[Mr. Harvey's prepared statement, with attachments, may be found in the appendix.]

Chairman LaFalce. Thank you very much, Mr. Harvey.

Our next witness will be Mr. Roger Little, cochair of the National Innovation Network, and president of Spire Corporation.

TESTIMONY OF ROGER G. LITTLE, COCHAIR, NATIONAL INNOVATION NETWORK, AND PRESIDENT, SPIRE CORP.

Mr. Little. Spire Corp. is in Bedford, MA. I have about 180 people. We are a high technology company which has been in business about 15 years. Our business started by doing Government R&D work and then trying to commercialize that. And I have been reasonably successful in doing that.

My message here today is that the SBIR program, the Small Business Innovative Research Program, is a very good one. I believe that the committee recognizes that, having extended the level of funding for SBIR for a number of years. But my specific recommendation is to put more resources into SBIR and to direct those resources toward the development of innovative products which can help American competitiveness in exports and in import substitution. I can give you some examples.

Included in my testimony is a map of the world showing where my company has photovoltaic manufacturing equipment. One of our areas of business is photovoltaics, the conversion of sunlight directly to electricity. So if you take something like this solar cell and you put it in the sun, you will make electricity. Under the SBIR Program, we were supported by the Department of Energy to develop technology for solar cells. Since energy is inexpensive in the United States, the market is naturally international. Something like three-quarters of the world's population does not have electricity.

So we have been able, as a small company, to go into the world and put equipment in North America, South America, and even Moscow. We are doing a good job in that respect having equipment in 20 countries. A lot more can be done. Right now most of the effort going into research and development of photovoltaics relates to utility grid applications. If we were to direct SBIR funds for product development for portable refrigerators for South America, South Africa, something like that, then we would get a lot more export result.

One of the weaknesses of the SBIR program is that it is dominated by defense R&D as you know. Seventy-two percent of our Federal R&D budget is for defense. It is very difficult commercializing defense technology.

My recommendation is to direct agencies, including Defense, which gives a lot of lip service to wanting to commercialize technology, to go ahead and address commercializing action through the SBIR Program.

One additional area we are in has to do with wafers, semiconductor wafers. This is gallium arsenide semiconductor wafers. The Japanese are big competitors. And if you go to the Defensive Atomic Research Projects Agency of the Defense Department, they are spending $50 million a year on advancing that technology for defense applications.

They have a viewgraph, the left-hand side of which is Defense requirements; the right-hand side says commercial requirements, to show the difference.

If we allow them to bridge from the defense requirements to the commercial requirements, we would get a lot more mileage and a lot more success in commercializing the technology and in preventing the Japanese from coming in here and taking things over.

Now, 1¼ percent, which is not a lot, of the Federal R&D is going to small business through the SBIR Program. We would like to see it increased in half percent increments per year over the next couple of years until it gets to 3¼ percent. And that half of the incremental increase be directed through the SBIR solicitation mechanism which now exists, toward products, again for export and for import substitution. We believe that a tremendous amount of innovative product development would come of it and we, as a Nation, would indeed become much more successful.

Another example. We have a process which makes the surfaces of artificial joints perform better, and here is a knee. One of the questions I have asked is why the Japanese knees are not competing in the United States. The answer is because our smallest size is their largest size. So if we were able to develop the tooling and technology, we might be able to ship our knees into Japan. This is the National Institute of Health SBIR program.

In summary, increase the amount of resources going into SBIR by swinging from other programs. We are not asking for new money. The basic legislation exists. We are not asking for a lot of new legislation. The mechanisms exist, the organization exists, these agencies know how to move this money now and get it to the right researchers, increase it that half percent, direct it toward commercializing their technology, defense technology, NIH technology, NASA technology, and we will mobilize small high technology businesses and make a contribution to this American competitiveness issue.

Thank you very much.

[Mr. Little's prepared statement may be found in the appendix.]

Chairman LAFALCE. Thank you very much, Mr. Little.

Our next and last witness will be Mr. Gordon Johnson, president of Johnson Associates.

TESTIMONY OF GORDON O.F. JOHNSON, PRESIDENT, JOHNSON ASSOCIATES

Mr. JOHNSON. Thank you, Mr. Chairman.

I think I am really here as the retired chairman and a founder of a company called LogEtronics in Springfield, VA. We are manufacturers of capital equipment and my remarks here draw upon the 30 years of experience in that business, building ourselves up to where 40 percent of our sales were exports by 1980. We have equipment in 90 countries around the world. We are about $30 million of sales and 250 people.

As I look back on how did we get there and figure how could we get there quicker, the ideas that I would like to discuss with you and propose to you here come from that kind of background and experience.

I think the basic issue has been described and I will not spend more time on it: Namely, we are living on borrowed time with borrowed money to finance consumption and not production. This is one of the most threatening, dangerous prospects for this country that I can possibly imagine, and we cannot continue going the way we are going. Something has to happen.

Fred Bergsten's point that we must increase our exports to get ourselves back in track I think is key. How can we have military security if we do not have economic security? And this administration is so occupied with military security they are forgetting the economics of the global marketplace.

We have a trade deficit. Sooner or later that trade deficit, caused by excess imports, is going to have to be paid for by excess exports, by more exports. We cannot go on the way we are going.

Where is the increase in exports going to come from? I do not think we can rely on the lower dollar as a panacea that is going to solve all our problems. My Japanese competitor spent 20 years making his product better and better and better with the currency subsidy that he had from his undervalued yen in world markets. Comparative advantage does not work when you have a currency with a life of its own, a value of its own, a monkey on my back that prices my products higher than his because of the currency exchange. He used that currency subsidy not to cut his prices; he used it to make his product better. I had to cut my prices and not do the product development, not do the marketing to stay even with him. and I am not going to win that back just because his price is now higher. Eventually, it will help over a long term. If I can get my prices back up again as a domestic manufacturer, I can begin to put more into R&D and more into product development again.

We are not a high technology company. We are selling, to the printing industry, equipment which is competitive around the world.

This country must look at where can we get our exports and small business represents a significant potential for increased exports. Yes, there are a number of small businesses out there fighting hard already and winning orders by the quality of their products, the newness, their special features. There are a lot more who are presently ordertakers who could be marketeers. They could do more and are going to have to do more, because if every small business in this country does not get out into global marketplace and compete, our foreign competitors are going to be there, and after that, they will be here. So the best defense is a good offense.

Our small businesses, all of us, have to get out and sell in foreign markets. And how do we do this? I do not think small business owners are lazy, dumb, ignorant, stupid. They are probably smarter than anybody in this room, including me, and with all due respect, the rest of you.

Mr. McDADE. I will sign up right now.

Mr. JOHNSON. I think there are very good reasons why a lot of them are not exporting. They happen to know that there is more risk, and that is personal risk. It is not like a large corporation where it is the corporation's money. It is my money, my wife's money in a sense. The front-end investment is greater. The hassle factor is higher. The obstacles across the board are much bigger. It is much easier to concentrate on the domestic marketplace, and most people do what comes easiest.

I came up to testify when the export trading companies were being considered, and I said I thought this was just more people wanting to put their hands in my pocket, the small businessman, to raise my prices, charge me for what their services were going to do for me in overseas markets. And in point of fact, the export trading companies have not caught on the way a lot of people hoped they would. And certainly I hoped they would, along with everybody else.

True, we must recognize that small businesses are disadvantaged in the global marketplace, U.S. small businesses, for a lot of reasons. That litany you've all heard before. But what I would stress is that those small businesses today, some of them, are going to be the big businesses of tomorrow. And any company with an export potential is a sunrise industry. It is not a targeted industry. When you help small business, you are not saying you are going to go help the shoe manufacturers, or going to help the telecommunications industry. We are going to help anybody who can compete in the world marketplace, and let the marketplace decide who is actually going to be out there and who is going to win.

Now it is not that government has not been trying. I have been involved for the last 10 years. I got involved in a U.S. Chamber Export Policy Task Force because they did not have any small business people there and needed them. I said I am not a member of the Chamber. They said come anyway. And I learned a lot in that experience. I have been active there in the Small Business Council, as well as in the international side.

I have served on the Export-Import Bank's Advisory Committee, one of three small business people on the committee. I was there for 2 years. They are really beginning to make some progress. For all the bad things you hear, remember these tend to originate in the past. I think you are going to hear good things. They are pushing very hard to create multipliers, not to do the work themselves, but to create multipliers out there in regional banks and trade associations and others who can get to small business. They cannot do it physically themselves. They do not have the staff, but they are picking up the momentum and I think you will see a lot happening.

We have had all these seminars, we have had instruction booklets on exporting, we have had trade missions, and I have been on one. I have been to a lot of the international trade fairs. The foreign market data reports, they are never detailed enough for what I need. The prospective buyer leads, they do not seem to fit my industry, my company, exactly. The foreign sales agent list, and on and on. There are all these helping hands and things in the store. But somehow they are not producing what we think they should be producing.

There are a lot of people out there who want to help me, but I have got to pay them in time, and often money, to help me. So the question is, I think, how do you get the small business owner's attention so that he can indeed be willing and interested in using some of these helping hands? There is a lot of help there for him once he makes the commitment to do something.

Until the president or the owner decides that we are going to do something in the foreign marketplace, foreign markets will always play second fiddle. The 60-cycle machines will always get done before the 50-cycle machines. The foreign travel will be done when it fits my schedule to do it as the president. The sales manager is usually too busy to go. So, it is usually the president who does the foreign marketing.

What happens when he gets back? He works on all the other things that are calling for him and did not get done while he was away. Foreign markets play second fiddle in most small businesses.

We work with three Danish companies today. The sales manager there is the export manager. The domestic sales manager reports in to the export manager in a Danish company. It is not that way in this country.

How do we make the commitment? How do we get that commitment?

I think that you have to look at some meaningful financial incentives. One of them, and a good example, is the Shared Foreign Sales Corporation which Delaware is already promoting. They have a brochure. I am sorry I do not have one here to show you. But they have a brochure that they are out selling to any company around the country which says: "Come be a Delaware corporation and get a 15-percent Federal tax exemption."

Now the IRS does not like that, and I understand the IRS is trying to rule out the shared small SFSC.

But it is that kind of message that we are going to have to have, and the fascinating thing about that brochure is that that headline was written by a private sector firm seeking to make a profit, because the Foreign Sales Corporation, as probably you know, is a successor to a DISC. Both of those things are so complicated most small businesses cannot possibly figure out how to do it.

We spent $30,000 one year with Arthur Anderson to redo our DISC that had been set up by Price Waterhouse and I said to them, "$30,000?" They said, "Well, you would have lost your whole $100,000 that you had got deferred if we had not done this for you. Furthermore, we got you another $50,000 in deferrals, and so that more than covers the $30,000 you have to pay us." And I still do not know today what those changes were. It is too complicated for small businesses to understand.

So Price Waterhouse, in the case of the FSC, developed the software to be able to do all the calculations and figuring and reports and everything else that is required, and now all you have to do is go to Delaware and they have got the Price Waterhouse software. Price Waterhouse will make a profit, and the Delaware State export development people are going to be happy with more exports.

How do we do more of that? I suggest to you that you study the report of the White House Conference on Small Business. I hope you all have your copies of this book, that you have all seen it. It should be a dog-eared book in your office because this has an agenda for small business that I commend to you for the next 10 years. I hope we will have another Conference before then, however.

There are three international recommendations. One of them, number 35, deals specifically with exports. We did not fold it into the popular one for MITI or DITI, which is number five on the list, and which we all banded together to get something on the top 10. But number 35 is how to increase exports. One point is to improve the Foreign Sales Corporation and make it more attractive beyond the present FSC which is still complex without any real meaningful tax benefit.

The other one, the exciting one which I really want to discuss with you here, is the idea that what we should be putting together to get the attention of small business to export is an idea that comes out of something which has already been tried. Roger and Milton both talked about it; the SBIR Program.

The SBIR Program offers some incredible opportunities for Government and small business to work together in ways that small business can cope with, and in the past, that was a very difficult thing for Government to do. The Government employee is often someone who is here to help me but somehow never usually does. The SBIR is an exception to that rule, because in the SBIR approach, Government does not come up with all the answers and write voluminous specifications and put something out to the low bidder. In the SBIR approach they set a fixed amount of money and then they let the small business person write the specifications. Instead of the Government figuring out the answer, they ask the small business person what would he do in his business to really solve this particular problem.

And you have seen some solutions that have come up in the Department of Energy's defining some problems and small business responding. That is a fantastic approach. And we could do that in the export area. It will take some adaptation and some changes to do it, but the Government found a way to work with small business in the SBIR Program. I hope you do not rest on your laurels feeling that you have implemented now one of the White House Conference recommendations when you renewed and extended the SBIR Program. That was not the purpose of the recommendation that is here. This says you should not only renew it, which we were concerned about; it says you should improve and expand it, and I hope that is a remembered point.

I see, Mr. Chairman, that I am running to the end of my time, but before you will have to interrupt, let me just say an export increase program, you might call it a small business export innovation award program, operating on the same lines as an SBIR Program for research and development, wouldn't involve any new appropriations if you can do it on a set-aside basis, and serve as a marketing vehicle, a tool for all of these export trading companies and people to use to get my attention, or the small business. If we do it right, we will get 8 to 10 proposals for every award winner. That is a fantastic multiplier effect on the way the program works.

We should set up a program with 100 to 200 awards, $25,000 each in the award, with the requirement let us say for an equal matching amount of new funds for export promotion. And remember, these are marketing dollars, not R&D dollars, or they could be

R&D dollars if that is the best way to increase exports, but listen to the small business on what it thinks it could do and pick the best of those proposals.

So to conclude, three objectives: A program which would create awareness. Remember, nothing happens until somebody sells something. Second, it would get specific increases in marketing exports by the winners of the awards. And third, you would use the knowledge and the experience gained; the winners would share their know-how and what they did with other people and become again multipliers of the benefits of exporting for small businesses that are not doing it.

So the first thing you have to do if you have a lot of products in the store that you want to sell to small business is to get him into the store in the first place. You have to have something to get his attention.

Mr. Sisisky does have a bill ready to propose on how to do a small business export innovation award program, and I commend it to you. It has most of the ingredients in it. It is borrowed from the SBIR Program. And I think something like that can make a real difference. We cannot just keep shouting from the house tops at small businesses that they have got to export, because it is not my imperative as a small businessman to export. It is my imperative to survive and grow, and I do not have to export to do that most of the time.

Thank you, Mr. Chairman, for the opportunity to be here.

[Mr. Johnson's prepared statement may be found in the appendix.]

Chairman **LaFalce**. Well, thank you very much, Mr. Johnson, and all members of the the panel. As someone who is the principal author of the SBIR bill and managed it on the floor, I am extremely interested in not just seeing its continued life, but to see it flourish. We will see what we can do along those lines. We will work with you and Mr. Sisisky to see if we cannot develop something.

I am going to refrain from asking questions at this time so that other members of the committee may have the opportunity, and so I will turn first to questioning to our ranking minority member, Mr. McDade.

Mr. **McDade**. Thank you very much, Mr. Chairman.

Let me begin by saying how proud I am to have my name associated with the work product that you have produced. What you have done is really an excellent road map for all of us that defines the incredible dimensions of the problem that we face. And, as was pointed out, I think very appropriately, perhaps it catches a bit of the tide that runs in the country today in the form of a growing awareness that until we solve this problem the country is going to continue to deteriorate economically. Mr. Harvey, I particularly appreciated your comments about what happens to future generations.

When I go back and talk to my people, be they in the textile business or be they in the electronics business, they talk to me about the inability to compete with foreign wage rates, inability to compete with government abroad that is organized exclusively for exports. And, indeed, when you look at our principal competitors and see them as nations really living with barren resources, a lot of them, but designed to structure their governments through export trade organizations, et cetera, to take the raw goods, to manufacture them at a wage rate and a productivity rate that is above ours and below ours in the other instance, and then to flood the world market, then one wonders how it is that we possibly do begin to compete.

Mr. Johnson, you sound like a lot of fellows that I talk to in my office, in my district office when they ask: How can I possibly get out and compete when I have to try to earn my sales dollar and my profit dollar right here?

Hence, the importance of the report that you have produced for us. It indicates that unless the Nation begins to make really dramatic changes in its overall organization to meet this problem, we are going to be talking about it for a heck of a long time.

I know this is a terrible thing to do, but the Small Business Conferences have always been geared to make hard choices, and I will tell you what I would like you to do for me if you could. You do not need to do it now; you can amplify it for the record and I would like you to try to do it as a group. Tell us the top 5, if you will, the top 10 recommendations that are extant in here. We have a limited amount of jurisdiction and, Milt, you sure know what that means when we talk about the jurisdiction of our committee. But we are not just a jurisdictional committee; we are a sounding board and that is why we are all here. We hope we have a voice that is heard throughout the Congress. I would like you to look at it from the standpoint of our jurisdiction, like the SBIR Program that we were privileged to work toward, and tell us what you think, in terms of our own jurisdiction in this committee and the room, and in the Congress in general, that we can perhaps promote more loudly as a sounding board, that you think we ought to set up as a goal for ourselves in this area in a prioritized way.

We would be very delighted to have that kind of additional input from you. Unless I am asking you to do something that is unreasonable, I would be very grateful if you could.

Thank you, Mr. Chairman.

Chairman LaFalce. Thank you, Mr. McDade.

Mr. Olin.

Mr. Olin. Thank you very much, Mr. Chairman.

I would also like to congratulate the panel. I found all of your testimony to be extremely interesting and very pertinent, and I congratulate you for it. I would like to address something along the lines that Mr. McDade mentioned. I want to address this question to Mr. Lilley.

I have spent most of my life in a large business, but within a small part of the large business there was exporting. I certainly have come to the conclusion, as Mr. Lilley said, that America can compete. Much of America is competing. My experience has been that if the management or president of the business decides he is going to be competitive and then if he can get together the resources and have enough perseverance, if he can last through the investment period, that he can compete.

I guess my question to Mr. Lilley is this: What is your idea of maybe the two or three policies that the Congress could enact or encourage that would have the biggest effect on business managers and leaders to help their motivation to be competitive and also look at the international market? Or do you feel that the motivation is in pretty good shape already and we ought to leave it alone and let it work?

Mr. LILLEY. That is a good question, Mr. Olin. I think you see in a restructuring in American business that very large units are downsizing now, and you are seeing your growth in the small units and the medium-sized units, and you see a different management attitude often on the parts of those different sized units.

To go back to what Fred Bergsten said, that if we are to work our way out of this mess that we have to grow our exports. As to what the Government can do, I do not know where you start because it is such a big job. As Mr. McDade said a minute ago, there is no emphasis in the Federal Government as to whether whatever the Federal Government does is export neutral, export negative, or export promotive.

In the 1970's when we had an inflation crisis and an energy crisis, I managed an agency, the Council on Wage and Price Stability, and we started reviewing Federal regulations to see what was their impact on price enhancement. We found that a number of regulations which were very properly designed to protect, say the safety of a power lawnmower, were having inadvertently an enormous price-enhancing effect and inflationary pressure through the system and thus causing an inflation problem in the country.

Similarly, today with regard to exports, there are a number of tax, accounting, and a large number of off-budget regulations that if the Government really wanted to get serious and say that exports were something that we really wanted to do and organize ourselves like—I commend a book to you. It is called "America Versus Japan." The Harvard Business School has just published it, and they talk in the first chapter about how Japan has organized its government and society to export. And much of that organization is noncoercive in nature and is off the budget.

If we really want to do it, then we can move to make Government more pro-export, without being overly coercive. We have a Tax Code which encourages business to do things, and we have other regulations which provide other incentives. We just have not figured out what kind of policy regarding trade we want it to be. And if we start looking at that seriously, if we have to get ourselves to the level of exports that most people think we have to, then the Federal Government has got to do its part and agencies like the IRS, and the SEC, and FASB and people that live in their own worlds, which is basically a Fortress America world, they have got to be hauled in under another kind of trade-related microscope. That is not going to be fun in this town.

Mr. OLIN. Would these take the form of various types of monetary subsidies in one form or another, or are they other types of——

Mr. LILLEY. No, sir; I think it is the kind of bare-knuckle work that you see going on now where you have the Defense Department and the State Department warring with the Commerce Department and the Treasury Department over export licensing, and the Congress never likes to get in the midst of fights between agencies.

Mr. **Olin**. That is what you mean by off-budget. They would not affect expenditures or revenue basically.

Mr. **Lilley**. Some of the most sacrosanct agencies which provide both carrots and sticks to American business have got to be given a new priority, and that is to increase exports. And just as we started overhauling regulations in the 1970's regarding inflation until finally you had both Presidential candidates running on the platform—both candidates remember were mocking the OSHA regulation in 1976 that we are going to mandate portable bathrooms out on ranches and farms. That is the kind of thrust you people really should take if you want to motivate business to make it more profitable to export. And you do not have to do it, in large part, by going into subsidies, but you have got to do the tough, dirty work and that is take on the agencies which have their own agendas, their own constituencies, their own committees, and they are doing what they think is right for themselves and for the country. That is my thought.

Mr. **Olin**. That is a very interesting observation, a very tough order on us.

But thank you very much, Mr. Chairman.

Thank you, Mr. Lilley.

Chairman **LaFalce**. Thank you, Mr. Olin.

You know, one of the things that I worked on for the past 4 years—had reported out of subcommittee and full committee in the Banking Committee—was the Council on Industrial Competitiveness that could try to help make American industry more competitive. It is not a protectionist bill, not a bill that is going to involve any Government planning whatsoever, but a bill that simply gets Government, labor, and management together, not to discuss great issues of trade policy, not to discuss anything other than how can we help ourselves, how can we become more competitive.

I think that is somewhat along the lines of what you are talking about, Mr. Lilley, and I notice that it was one of the recommendations of the national commission, Mr. Harvey.

Mr. **Harvey**. It just happens to be in the report, "Making America Work Again."

Chairman **LaFalce**. Right, that is what I meant.

Mr. **Lilley**. Mr. Chairman, my staff has made it very clear to me of your interest in that mission.

Chairman **LaFalce**. Mr. Campbell.

Mr. **Campbell**. Thank you, Mr. Chairman.

And thank you, panel, for the informative testimony and providing some of this very fine literature.

A couple of points, and maybe a couple of questions: I personally think that one of the problems, we speak of Japan very often when we talk about competitiveness, and I guess obviously because that is where we have the biggest trade deficit. But one of my problems has always been with people who develop theses on how to deal with Japan, as they have never been there. And they rarely have an idea of Japanese business practices, or how decisions are made in the business community over there. Sometimes go with a weekend trade show and come back with the taste of sushi in their mouth, but it does not translate very well in dealing with Japanese businesses.

On page 19 of this booklet, there was a statement at the bottom on discriminatory regulatory standards. That was interesting to me. It says, in part, that new products are often blocked in Japan from being introduced until Japanese patents can be taken out and Japanese similar products can be brought on line.

I lived in Japan a number of years and worked for export companies, and speak Japanese, too, so I think I know the difficulties better than most Americans do, in working over there, and I just thought I might tell you that the years I worked there, I used to come home once a year. And I used to ask that company, the officials of the company, what you like to bring me—what would you like me to bring you from America, souvenirs, American golf clubs, something of that nature. And you would never guess the thing that they always put at the top of the priority list to bring from America. It was Sears & Roebuck catalogues. That was always what they asked for first, the latest catalogues of Sears and Macy's and whatever I could get.

So I suppose, somewhat tongue-in-cheek, I thought maybe we ought to have an amendment in the trade bill restricting the export of Sears catalogues. But on a more serious note, I read an article the other day when I was flying back here. I believe it was in the U.S. News & World Report, about counterfeiting American products, and that article estimated it is now a $60-billion-a-year industry and has caused the loss of 750,000 American jobs through copying, plagiarizing, and counterfeiting brand names, copyright names, and trademarks.

It is a fine line between protectionism and fairness, it seems to me. And I do not know how to address that. It seems that some of the things we have to do are really, if we are going to correct that, are punitive rather than dealing in a competitive solution.

But I wanted to ask, I guess it is Mr. Little, who showed us some very exciting products there, and I noticed in your testimony, you have a map of the places that you now sell and distribute, and you have several in Japan. I wanted to ask you, how do you protect those from going over there and having them come back a year later with a minor change and the word Mitsubishi stamped on them?

Mr. LITTLE. That is a danger. I have shipped equipment into Japan, and have found similar equipment for sale from Japan in the past. I am running a sort of a tightrope now with one of our products. It has to do with these wafers, and I have, as of yesterday, made an agreement with the world's largest supplier of these wafers in Japan, and I have given him an exclusive for Japan to go sell my wafers.

Now, he has told me that as soon as he can, he is going to make his own wafers, and I told him——

Mr. CAMPBELL. At least he is up front with it, is he not, that he is going to rip you off?

Mr. LITTLE. And I have told him, well, you will not learn how to make those wafers from me. So we are going to see who wins in the long run.

But it is a very difficult proposition. You have to be on your toes, and you have to stay ahead of them.

Mr. CAMPBELL. Well, yes, that, and I believe there really is not a finite time. When we say we are back on track with competitiveness, now that is an ongoing thing where you have to continually research, you continually have to move ahead and do things of that nature.

But specifically to the question of counterfeiting, I understand many things are being counterfeited from that article I read, such as some of our medicinal supplies, things like Levis, brand name Levis, Stetson hats, and so on. They are shipped over here, and then forgeries of the American trademarks are then sewn on, paper tags are taken off, those are sewn on, and then those are marketed to an unwary public who thinks they are getting a brand name which they have come to believe is quality and probably safe because of the millions of dollars American industry has spent on those brand names.

How do we do, how do we handle that without some kind of, if I can use the word, protectionism?

Mr. LITTLE. Well, in my opinion, you do have to have protectionism there, but is that not a Hong Kong problem, by the way? The Japanese do not do that.

Mr. CAMPBELL. I do not know. The articles did not say who; it mentioned several countries.

Chairman LAFALCE. It is not exclusively Hong Kong.

Mr. CAMPBELL. I do not think they are the only ones.

Mr. LITTLE. But it is really not something that I can really speak to. My approach to life is to run faster and try to stay ahead of them.

Mr. CAMPBELL. It is like running when they are behind you with a bicycle. Yes.

Mr. HARVEY. Mr. Campbell, if you would not mind my making a comment about that, one of the commission's recommendations is that intellectual property rights be included in the current round of GATT negotiations. Now, I think the commission's intention in discussing intellectual property rights was that such things as copyrights and patents on products would be respected in international trade.

Currently, an American firm that invests billions of dollars developing a new software or a new technique really has no recourse if the Taiwanese or the people in Hong Kong steal the process or steal the software.

Mr. CAMPBELL. That is what I understand.

Mr. HARVEY. I am not terribly worried if a yuppie buys a Gucci bag and finds out it really was made in Hong Kong with a false brand name put on it. But these other issues of software and technology and manufacturing processes I think can be protected through copyright and through patents.

Mr. CAMPBELL. You think they can be expanding the GATT, the scope of General Agreement on Tariffs and Trade?

Mr. HARVEY. And that is why the commission made that recommendation in its report, because right now there is no international sanction against that kind of product piracy.

Mr. CAMPBELL. As I understand it—correct me if I am wrong—if you come up with a new product like that, and you want to protect it in those countries even, you have to get virtually a patent in every country. Is that correct?

Mr. HARVEY. I believe so.

Mr. CAMPBELL. Otherwise, you are pretty much at the mercy of whomever is in that country who wants to try to copy it.

Mr. STEWART. Legally, this is about the stickiest problem that faces us. What paralyzes us is the word protectionism, and fear of retribution. And in my view, we have overdone our deference to other countries about this. Until we have international rules that are enforceable about this matter, you are not going to substantially expand American exports in many technology areas, except for products where the company that develops them is confident that it can do what Roger talks about—stay ahead of the market and take it for granted the product is going to be stolen.

There are companies that can do that in the American Business Council and other kinds of companies. There are many, many more companies that cannot do that, where they have to turn to laws and regulations which do not exist, or which are so costly to utilize that they are priced out of markets.

Mr. LILLEY. You know, I think we, if I could just add, I mean, I think it makes us feel better to say that we are being hurt by nasty people, but one of the bigger problems was here at home, was that we had laws on the books here until a year or so ago which prevented this country from being a party to the Berne Convention, and therefore we were not able to bring intellectual property protection to GATT. And until we made those changes—it involved union regulations in printing—we have been part of that problem, too.

Mr. CAMPBELL. Thank you, Mr. Chairman. I might just, in closing, say that a couple of members have asked for any information on several other subjects that you might have that you could provide. If you have any information about that, or suggestions about what we can do from this committee——

Mr. LILLEY. We do.

Mr. CAMPBELL [continuing]. To protect that or to expand GATT, some way to address the problem of counterfeiting, I would sure appreciate it, and I think the other members would, too, if you would send it to us.

Mr. STEWART. I have to interject, Mr. Chairman, if I may, this comment. I am glad you mentioned GATT. This committee, more than anybody else, kept GATT from overruling every set-aside program in the United States for small business. At the Tokyo summit, our own negotiators let it happen. That is how insensitive they were.

When the treaty came to the Senate, this committee, fortunately, found out about a provision in the treaty, and all of a sudden, nobody downtown was home. We never did it, nobody was there, we never—the same old story.

I am making a point. The point is——

Chairman LAFALCE. Could I just interject, because I was chairman of the subcommittee at that time that had responsibility for procurement. At that time, I contacted Robert Strauss, and he testified before our subcommittee, and between the time of contacting of Mr. Strauss and the time of his testimony, the GATT had been renegotiated with respect to the small business set-aside.

Mr. STEWART. They stayed up day and night to renegotiate that clause in the treaty, because this committee found out about it.

Chairman LAFALCE. Hopefully we helped the picture.

Mr. STEWART. There is a lot of history in this committee that the general public does not know.

The point I want to make is that without the kind of vigilance that can come from an informed small business community, you are not going to deal with that problem or any other. Small business does not give a damn about exporting. Gordon has told you why.

In preparation for the 1980 conference, my secret weapon was my wife. She ran the delegation from Arizona. She convened a meeting of the delegation, because we have a guy in Tucson who is a brilliant exporter. And she said, you have been so successful. I want you to tell everybody else about it.

He talked for about 40 minutes about what regulations you comply with and what not. When he finished, somebody asked him, well, would you do it again, go into exporting.

And he stopped and he said, you know, I do not think so.

Now, I think, in a country where—I used to make speeches for the Government on this subject all over the country, when I could not avoid it. Export, export, export, all the baloney we threw at them. It was always a guy, I was talking to people I knew, who came up afterwards and said, now, come on, the rest of those people they send out here we do not know; we know you; you know better. If I get $200,000 more in credit from my bank, I am going to open a plant in California, or Maine, or wherever he is.

That is the key to the whole thing, I have tried to say that. Our market at home is enough for the normal small business person. He does not need to go abroad. He does not want to go abroad. We need him to go abroad. The Government will not get the private sector, here as anyplace else, to take any risks unless it takes the first risk.

That is why the SBIR Program works.

Two points. That is why we need an international convention, because until there is a consensus and a constituency out there to support you when you want to do something that makes sense, you are not going to get it done in the Congress. The SBIR bill was referred to seven committees, the chairman will tell you. It took a miracle to pass it. The miracle began with a constituency that was there and was organized. It is not there for foreign trade on anything having to do with small business. And it will not be there until we get a chance to develop a leadership.

I think the first thing we have to do with that is to get them together with small business people in the rest of the world.

Chairman LAFALCE. Thank you.

Mr. Mazzoli.

Mr. MAZZOLI. Thank you, Mr. Chairman.

Let me sort of frame the issue as I see it. Maybe I am wrong, but it looks to me that if you were to take the issue to the floor, there would be a uniform "yes" that there should be some assistance to small business in capturing foreign markets or getting involved in foreign trade and the creation of jobs. But when you start the particularization of it—should you start service jobs which do not pay but minimum wages, should you start plants which do not unionize and are not subject to organization—then you find a lot of very different opinions.

So, let me just ask this question: Is everyone on the panel in favor of a Cabinet-level board or department of international trade? Starting with Mr. Bergsten; are you in favor of a Cabinet-level operation like that?

Mr. Bergsten. I am in favor of consolidating the trade policy functions we have in the Government, but I do not think the way to do it is a Cabinet department. Trade is too important. The Cabinet department will be one among equals, and a lot of different parts of government are inherently involved in trade.

Therefore the Congress was basically right in 1962 to create a trade coordinating and negotiating office in the White House, and to strengthen that function in 1974 and again in 1979.

My proposal, and it is based on a study carried out by one of my colleagues at my Institute—we published a book on it 3 months ago—is to expand sharply the responsibilities of the United States Trade Representative in the White House, assimilating all trade authority under him. Now, you do not want to put a huge bureaucracy in the White House so you have a trade administration outside the White House, but reporting to and directed by the USTR. I think that is the way to go.

I think your other big problem, and the one I emphasized in my remarks, is that our trade balance has been undercut not by trade policy but by macroeconomic and monetary policy. So you have to find a way to make sure that the errors of the first 5 years of this administration—ignoring trade, letting the dollar soar, and giving us a $150 billion deficit—are not replicated.

What that means is setting up a mechanism to assure that trade and monetary concerns are viewed indivisibly in the future. There are provisions which the chairman of this committee has put forward successfully in the House Banking Committee—called the Competitive Exchange Rate Act—which would bring the exchange rate issue out of the closet, and require that trade considerations be factored into exchange rate and monetary determination across the board. And that, to me, is the second and equally critical step to achieve what you are trying to point out.

Mr. Mazzoli. Mr. Johnson, from what I gathered of your testimony, you did not think much of what was going on. As a small business, you did not think that help was available to you, or you would have to pay for it, or something. Do you think a Cabinet-level board of international trade, or do you think something like Mr. Bergsten has talked about, is a better way? Or do you think that neither should be, and just let you guys thrash it out and see what happens?

Mr. Johnson. The answer is absolutely "no" to your last alternative.

Mr. Mazzoli. All right, so it is either Cabinet-level or some sort of coordination?

What I got from your testimony was the impression that nobody offered you much help, and that if they offered it, you would not probably take it.

Mr. JOHNSON. This was a major issue for the White House Conference on Small Business. It was fifth-ranked among all the things that they could have chosen. It was the heading under which we grouped a number of States, grouped their various recommendations as to what was needed in international trade for small business.

And it came from the fact that I think everyone there recognized that this Government, this administration, has not given priority to our global competitiveness in the decisions they make on budgets. They are all prepared to do everything in defense, but nothing for the economy that underlies it.

Mr. MAZZOLI. Well, how would they do it, though? You did not answer. Do you think there ought to be a Cabinet-level Department of Trade?

Mr. JOHNSON. Yes.

Mr. MAZZOLI. How do you see that Cabinet-level department pulling together all the strings? Do you see them going to bat in favor of creating jobs that are not going to be organized, or in favor of service-type jobs which people are now scorning? How do you see that Cabinet-level department operating?

Mr. JOHNSON. Pulling together all of these different functions that are spread around in the Government. You have got to go here, there, and the other place to get answers to any question.

Mr. MAZZOLI. You think the Small Business Administration ought to be phased into that?

Mr. JOHNSON. Well, the Small Business Administration is involved with a lot more than just international trade.

Mr. MAZZOLI. OK.

Mr. JOHNSON. I mean, the liability insurance problem——

Mr. MAZZOLI. So all aspects of foreign trade should be melded into the big one? Is that your idea?

Mr. JOHNSON. Yes, right.

Mr. MAZZOLI. Mr. Little, what is your feeling on any of these things?

Mr. LITTLE. My view is you should have a Cabinet position. It is time to raise concerns.

Mr. MAZZOLI. Were you for the Cabinet-level Department of Education?

Mr. LITTLE. Pardon me?

Mr. MAZZOLI. Were you for creating the Cabinet-level Department of Education?

Mr. LITTLE. I was not worried about such things.

Mr. MAZZOLI. If someone had worried you with it, what, would you have been—for it or against it?

Mr. LITTLE. Department of Education?

Mr. MAZZOLI. Yes; you would probably have been against it?

Mr. LITTLE. I do not know about that, but I am in favor of the trade——

Mr. MAZZOLI. Give me your thoughts about the bureaucracy problem.

Mr. LITTLE. The bureaucracy problem only gets worse as you go deeper.

Mr. MAZZOLI. Does it get worse as you go higher?

Mr. LITTLE. Well, I do not know. I am very much involved in renewable energy, and there is a committee called CORET—Committee on Renewable Energy Export Technology. And this is led by the DOE, and has got AID and OPEC and Exim. And these people tend to thrash around a lot, but not accomplish a lot. And I think it is because they can only talk at the level at which they coordinate.

And I think if you had some authority——

Mr. MAZZOLI. At the top?

Mr. LITTLE [continuing]. For AID, which represents the Defense Department, to buy photovoltaic products for export that would make sense for instance.

Mr. MAZZOLI. Mr. Stewart, how do you see it? Now, you have been around a while, you are an old hand, I guess you would say.

Mr. STEWART. I spent 3 years, Mr. Mazzoli, following the recommendations of what we used to call the second coming of Herbert Hoover, the Hoover reorganization programs, which, among other things, dealt with this subject.

Mr. MAZZOLI. Yes.

Mr. STEWART. I think no fewer than nine Presidents in my lifetime have wanted somehow to consolidate foreign trade matters in one Cabinet department or something, anything. I do not think any one of them succeeded. I do not think any one of them is going to succeed.

As long as you have the Defense Department, the State Department, the Treasury Department, Eximbank, all of the—the Fed as a statutory independent agency and congressional committees committed to specific parts of the subject—I mean, you asked would you be in favor of putting SBA in there, my answer is absolutely not. We fought tooth and nail to keep it out of the Commerce Department. We know it will get buried.

Mr. MAZZOLI. Yes.

Mr. STEWART. We fought to create this committee, to create the committee in the Senate. I am making a point. What the President wants is what matters. What the outfit is going to do is what matters. The organization structure is secondary.

Mr. MAZZOLI. Yes.

Mr. STEWART. And really, when you decide what you want done, and you get a President who agrees with you, I think you may get such a department.

Mr. MAZZOLI. Good. Mr. Lilley, next time you see Lee Brown, give him my very best wishes.

Mr. LILLEY. Well, Mr. Mazzoli, I want to tell you something. We have been talking about fairly light things here, and I want you to know something very serious. Your colleague, Mr. Campbell, made a major misstatement when he said that the most desired American product in Japan is the Sears catalogue. By far and away, the most desired American product now is Jack Daniel's bourbon——

Mr. MAZZOLI. I am sure that Lee is going to be up here, you see.

Mr. LILLEY. Which is made in Mr. Mazzoli's district.

Mr. MAZZOLI. You are upholding your end of the bargain very nobly, I must say.

Mr. LILLEY. I want to reiterate what Fred Bergsten said. Look, we have got a problem here which goes across all parts of this society and every Federal agency, and it is no accident that every major congressional committee is involved in it. We ought to be. This is ruining our economy. Everyone has a role to play here if we are going to address this thing.

We have to address this problem like we addressed the energy problem and addressed the inflation problem in the 1970's, and if we do not do it, we are not going to lick it.

Mr. MAZZOLI. Yes; the department of government does not make a difference.

Mr. Harvey, do you see it as just something you could do with the current tools if there was the desire to do it, or the will to do it? You do not need a new apparatus?

Mr. HARVEY. Well, I think Milt Stewart, who is one of our commissioners, said it right. If the President wants to get something done in this area, he or she will see to it that something is done, whether there is a Department of Trade, or whether they do it through the United States Trade Representative.

I am more and more attracted to the notion, the more I have learned over the years about the domestic policy staff, and recently in the last couple of months, and I do not say this to be—just to make fun of a serious situation—of the national security adviser's role in the White House, of a role such as that—a national trade adviser who could knock heads in the departments and make sure that the issues that needed to be brought to the attention of the President were brought to the President.

Just one final comment. I used to worry about educational matters. So I did pay some attention to whether or not there should be a Department of Education. I thought the idea was a terrible one. I have long since changed my mind. It was one of the best things that ever happened to education in this country.

Mr. MAZZOLI. I think you would find a good argument. There has not been a whole lot more done with that department than when it was as part of HEW. It may have a little more target, but it also draws more lightning up there. And you can get a lot more done working the back halls than you can working the front halls.

The chairman and I were on a television show even yesterday, and we talked a little bit about this. The big issue now—and this is where I say small business is deified and castigated at the same time—is that you create jobs but you do not create the kind of manufacturing "jobs" that we have been used to. Therefore is it appropriate and useful for Congress, the country, to encourage the creation of these kinds of jobs? Are they in the national interest?

And with the chairman giving us 1 minute, may I start again with Mr. Harvey and work my way backward?

Mr. HARVEY. I am glad you raised that issue. Small business does not create only low paying service jobs or jobs in retail industries. We had members on this Commission from organizations such as Pacer, Inc., a high technology, high growth firm founded by Jack Rennie in 1970 with himself and a partner. It now employs 300 scientists, engineers, and highly skilled technicians.

We have small manufacturing firms turning out machine tools and dyes. Small business is a vast sprawling empire of things. To just smear small business with the brush that it is just carry-out joints is, I think, a severe disservice. I am glad you brought it up.

Mr. MAZZOLI. Thank you. I would like to hear more about that at some point. I think it is going to be a big issue. Mr. Lilley?

Mr. LILLEY. I do not think the type of business, whether it is high technology manufacturing or a type of service company, is size related. I think it is more the type of business that the company is performing that really relates to the wage level.

I think you are seeing in small and mid-size businesses representative units of GNP. If you will pull out the appendix of our companies, some are very fast growing companies. I think that is not a problem for small or mid-size businesses.

Mr. MAZZOLI. Mr. Stewart?

Mr. STEWART. I think Jim Harvey is dead right. I do think that the Government and Congress can be very selective about what they want to stimulate. And I think they often are not.

Industrial revenue bonds are the clearest example. They were used by franchising fast food outfits even though many Members of Congress who supported them did not intend that. It should have been drawn better. And then we wind up throwing the whole thing out, which we should not have done.

The same thing has happened again, and again, and again. If you leave loopholes for people to create low paying jobs, they will do it. Let me just talk about the SBIR Program.

A perfect case in point. What you get is a range of wage level jobs. High level, mid level, low level. And lead to manufacturing jobs.

Mr. MAZZOLI. Mr. Little.

Mr. LITTLE. Certainly, small high technology businesses create jobs which are much more highly paid and requiring more education. Especially from an export point of view. You cannot export hamburgers. And I think that high technology is really the way to get your share of the export market because you can bury your product in technology which needs to be duplicated to duplicate your product. So I think it is important.

Mr. MAZZOLI. Thank you. Mr. Johnson?

Mr. JOHNSON. I am not sure that I understood your question.

Mr. MAZZOLI. Basically I am saying that there is a kind of a natural suspicion of job creation in the small business sector because the jobs they create are not usually organized and they are usually, as the saying goes, not highly paid. And I am asking: Is it therefore in the national interest that this committee or any committee encourage the formation of those kinds of jobs?

Mr. JOHNSON. Certainly it is in the interest——

Mr. MAZZOLI. If you attack the premises, that is fine, as Mr. Harvey did. Or in effect tell me I am wrong, or tell me I am right, or tell me something.

Mr. JOHNSON. I think it is undoubtedly true. Large corporations pay more than small businesses do. I had great difficulty trying to recruit from DuPont or Kodak, our major competitors, when I would go in once in a while to try to pull somebody out. The people we had were there because they liked the freedom of being in a small business and we could not pay as well as the Kodaks and the DuPonts do.

Mr. Mazzoli. So you think it is in the national interest? You think there is nothing wrong with it?

Mr. Johnson. I think it is very much in the national interest. We worked harder, did more, moved faster, did all kinds of things. We sold 74 percent of all the automatic film processing machines and daily newspapers. And Kodak, DuPont, and somebody else shared the rest. It was not the salaries of our people that made the difference.

Mr. Mazzoli. I think somebody said earlier today that some small businesses can turn on the dime and can react more quickly, which helps. Finally, Mr. Bergsten. I thank the chairman for his indulgence.

Mr. Bergsten. I will give you a stunning statistic. Over the last 15 years, as somebody mentioned earlier, the real wage in the United States remained about constant and we have created over 30 million jobs. Over the last 15 years in western Europe, the average wage has risen 40 percent and they have lost 2 million jobs.

There seems, in the real world, to be a trade off between the average wage and the ability to create jobs. So the only answer to your question is, compared with what. Sure, if we could have 30 million jobs and a 40-percent higher wage we would all love it. But in the real world there is a trade off and I think the American experience is better.

Mr. Mazzoli. I thank you. Thank you Mr. Chairman, for your patience.

Chairman LaFalce. Thank you. I do not want to delay this much longer. Just a couple of points. Mr. Bergsten mentioned the Competitive Exchange Rate Act as part of the banking bill. In testimony before the Banking Committee, he did indicate that it was perhaps the most important portion of the entire trade bill. I wish more of the colleagues were here to have heard the discussion.

With respect to the Department of Education and whether we should have had a Cabinet level or not, it is pure and simple a question of whether you are a member of the AFT or the NEA. The teachers know best. They should be for it, they should be against it. It just depends upon which union or association you belong to, which points out something else.

Organization sometimes is not nearly as important as what the President wants, what does the person in charge want.

I tend to agree very much with Mr. Bergsten though, that if you have a Department of Trade, then you will have a Department of State. If you have a Department of Commerce, then you will have a Department of Treasury. What you really need is the President to say, my USTR is going to knock all your heads together in order to make us internationally competitive. And we have not had that.

I think maybe the closest we came to it was when Bob Strauss was USTR. He probably had as much stature as anybody who ever filled that office. So you need stature, it seems to me. You need clear cut legal authority, too. More than anything else you need not only the backing of the President, but you would need the public recognition that you have the backing of the President in order to get this job done. Those are my thoughts.

Now, having made those statements, let me ask just a few questions. We have limited legislative jurisdiction in this committee.

We would like to come up with a small business title to the bill. One thing we could do is try to bring about—through this title—reports on subjects that are beyond the legislative jurisdiction. SBA can report on the Foreign Sales Corporation, the changes that should be made. We will certainly consider all of those things.

But in Mr. Harvey's statement on page 8, he said that only 1 percent of the SBA loans were used for exporting between 1983 and 1986. And I found that rather intriguing. Do you have anything more to back that up? Do you want to flush out that concept a little bit more?

I am just wondering if we ought to in some way encourage SBA to become more involved in loans for the purpose of exporting.

Mr. **Harvey**. Mr. Chairman, that evidence was collected at the Carter Center hearing, and also in the course of an interview I had with somebody from the Office of Trade in the Small Business Administration about a year ago.

The attitude at the Small Business Administration with respect to trade is that the loans they make they will make as they come into them. So, the small business owner comes to the SBA with a guaranteed loan that he wishes to use for exporting purposes, they will approve that. And basically the attitude is that nobody is coming to us. It really confirms what Mr. Johnson was saying. Nobody is coming to us and asking for loans for sales overseas.

My own view is that it would be helpful to encourage it. But there also has to be some sense in which the Government shares the risk with the small business owner.

Chairman **LaFalce**. You share the risk when you guarantee the loan. That is one thing that you surely do. There are other ways of sharing risk.

Starting with this point though, you are suggesting that people are not coming in and asking for that type of loan. It could be just a question of how you categorize it. Somebody might come in and ask for a loan for manufacturing purposes. And they would say well, that is not an export loan. But yet, unbeknownst to you, this person is exporting 25 percent of his manufactured product overseas. So, you just may not be measuring it accurately. That could be a problem, but let us not get into that.

What I want to get into is this. Milt, you said you have to develop a constituency because you do not have this demand right now for the small business community to access the international marketplace. But in making your comment, you were referring to 1980. And I think it was Mr. Johnson who, when he was talking about the White House Conference in 1980, said nobody was interested in exports.

But in the White House Conference on Small Business of 1986, it was the number 5 recommendation that at least had to do with the subject of exports. That is, called for the creation of a Department of International Trade. So what happened between 1980 to 1986 which made the White House Conference more concerned about the subject of trade? Is there now some burgeoning movement on the part of the small business sector that says, we do want a part of it?

Do they know by osmosis or implicitly what Mr. Bergsten said, that if there is going to be a future we have got to participate in that international marketplace? Is the time ripe for us to do something? And if so, what?

Mr. STEWART. First of all, on the narrow question, is the time ripe to do something with SBA. As a courtesy we have a new Administrator who is to be confirmed. I do not know what his priorities are going to be. I do not know if he is going to be free to set them himself. I think you are going to have to wait.

I went to the trouble of talking to perhaps a half dozen bankers in my part of the country before I came here. I asked about two things, the Export Trading Company Act, and about what are they hearing about the need for loan guarantees.

The answer on the first thing is that if you had started out intending to make sure that small business was disinterested in something and never paid attention to it, you would have done it just the way the Export Trading Company Act does. An obvious point.

If you tell a small business person this program is intended for you, fast growing mid-size companies and General Motors, he immediately translates that into this is not my program. It is not for me. If you do not call it small business they are not going to listen.

Chairman LAFALCE. On the first hearing on the subject of export trading companies I authored the bill that was initially suggested by the Carter administration, and I authored the bill that was suggested by the Reagan administration within the Small Business Committee. We could not get hearings in the Banking Committee. I had hearings in the Small Business Committee. And that was my intent. And we tried to do it.

We are going to try to come up with some new language in the banking title to emphasize that.

Mr. STEWART. Good. Now, as to whether there is a need for the money, I will tell you what I was told by commercial bank loan officers. They say if you ask people, "Do you need guarantees for export?" They are likely to say, "No." That conceals the fact that they do need guarantees for loans to strengthen their balance sheets to make export activity bankable.

The distinction to be made is we do need guaranteed loan programs, absolutely, to strengthen the company's balance sheet. To carry on the specific activity, my suggestion is that you look at a joint Federal/State program. Take a look at what Delaware is doing and what California has done. The States are a potentially great resource. And they can do some things better than the Federal Government.

SBA is a much burdened agency. It has just been through a terrible trauma. There are a lot of scars about it.

Chairman LAFALCE. Just so you know where I am coming from when you mention State agencies, one of the things that I want to do is use SBDC's to help promote exports. That would involve the States too.

Another thing. You are talking about long term capital. I do not know whether we can do it as part of the trade bill because maybe it will have to fly on its own. I hope we can do it in a bipartisan fashion. But we have got to develop a secondary market for small business loans. I am not talking exclusively about government guaranteed loans. I am talking about developing a market for industrial mortgages, a secondary market for industrial mortgages.

Because you now have a secondary market for just about everything under the sun except for that. I think you need some Government start-off agency to just get off the ground. We are even talking about a facility for the Third World debt that is to improve the secondary market for that. We ought to be talking about it for the small business community, too.

Let me ask this: In Mr. Harvey's testimony he said that the Export-Import Bank, which finances the sale of American products abroad, has not used the full amount of loans and guarantees for small firms authorized by Congress.

Mr. Johnson, you were on Export-Import's Council.

Mr. JOHNSON. Advisory committee.

Chairman LAFALCE. Advisory committee. And you said they were not doing too good a job. Are they doing a good job now? Is Mr. Harvey's comment out of date, or if the Export-Import Bank is improving, do they still have a way to go to reach the congressional mandate? And, of course, the congressional mandate is a floor rather than a ceiling.

Mr. JOHNSON. The figures were never very clear as to just what that mandate applies to as to guarantees and the direct loan program, medium/short term/long term, etc. And I think overall the Export-Import Bank statistics show they are complying, if you include the loan guarantee insurance, the risk insurance which is basically FCIA, there, small business is a very big participant. The direct loan statistics show that, the dollars are probably not up to the 10 percent. But I do think if you go line item by line item you may not hit 10 percent on every line item, but you will hit well over 10 percent in total.

I think the insurance program is a very meaningful one for small business. And they have broadened that so that you can——

Chairman LAFALCE. Is there anything we can do with that legislation to enhance the small business community's access to EXIM's programs?

Mr. JOHNSON. In terms of new legislation you can keep hammering on the 10 percent. There is a real awareness in the people there that their mandate is to go out and help small business. I think whether or not you can, what new legislation might be. Maybe Fred has some information.

Chairman LAFALCE. I do not know that the Export-Import Bank has the delivery service capacity.

Mr. JOHNSON. They do not.

Chairman LAFALCE. So you have to really have them teamed up. What I am thinking of is teaming up SBA to make SBA a delivery service entity for the Export-Import Bank in some manner. I am not sure what would exactly be appropriate, or how. But SBA is all over the country.

Mr. JOHNSON. Eximbank set up the National Machine Tool Builders Association as a delivery vehicle.

Chairman LAFALCE. Maybe just to let the SBA give counsel and advice and prepare applications for assistance for the Export-Import Bank, in addition to helping them prepare applications for SBA assistance. That is one possibility.

Mr. JOHNSON. I would suggest that encouraging them to work through multipliers as they are doing with the National Machine Tool Builders, and giving them authority to delegate. They are unwilling to delegate the authority out to make these small decisions.

If you could give them the authority to let the National Machine Tool Builders Association do loans or do within a pooling and inform Export-Import what they are doing, but not have to send all the papers back into headquarters in Washington. They are moving to set up the Machine Tool Builders to organize their small business members so they will deal with these. They are getting training programs from Export-Import on how to do it.

So the industry association itself is going to be out there as a multiplier for Export-Import. But then all the papers still have to go in and go through a whole lot of Government approvals processing before it can happen.

That is an example of some of the new things they are trying.

Chairman LAFALCE. OK. Fred.

Mr. BERGSTEN. The other way to get more mileage out of your 10-percent rule is to increase the base against which the 10 percent applies. Direct loans by the Export-Import Bank now total $1 billion or less. In 1980 it was $5 billion, at a time, incidentally, when U.S. exports were booming.

If you increase the base fivefold your 10 percent is worth five times as much. And my general recommendation, as part of the overall marketing push and re-entry effort by the United States in world export markets, is to sharply increase the role of the Export-Import Bank in magnitude and push it into a leadership role in this whole effort. That would bring your 10 percent to a much more significant absolute number and enable you to do a lot more with it even if the percentage itself remains unchanged.

Mr. JOHNSON. That is a frightening statistic because I can remember going in to meet with Mr. Stockman, Mr. Meese, and Mr. Brock with a small group, and urging the renewal of the Export-Import Bank reauthorization. And $5.4 million was the target and Mr. Stockman was going to cut it to $3.7 million. And today it is down around $1 million. And we have got to really get at why we are not doing more.

Chairman LAFALCE. Their initial position was to eliminate the Export-Import Bank, as you recall. The unilateral disarmament in international trade.

Milt, what did we do, either to or with the SBIR Program or how do we use it as a a stepping stone, to pick up on some of the ideas that Mr. Little and Mr. Johnson talked about. Should we just come in with something as a new program, if we are going to come in with something, separate and apart from the SBIR Program? Or should we build on the SBIR Program and give it an additional export tool and percentage? An additional half percent which would be exclusively for the purpose of exports?

How would you proceed if you were me?

Mr. STEWART. I appreciate, Mr. Chairman, your asking. We both know you know a lot more about this than I do.

Chairman LAFALCE. I fooled you.

Mr. STEWART. You have to because my answer is you have to do both. And you have to see which one the chambers, both of them will buy and which one will go downtown. I really think these gentlemen have presented two good ideas. I think one of them, Mr. Little's, can be a specific expansion of the existing program directed in this way.

Gordon's can be a new program using the same principle.

Chairman LaFalce. He was talking, Mr. Johnson, primarily about marketing.

Mr. Stewart. That is right. He is not talking about R&D dollars.

Chairman LaFalce. I know.

Mr. Johnson. That would be product development and application of——

Chairman LaFalce. How much money would we be talking about? Big R&D dollars or big procurement dollars. We are not talking about that big of a base for marketing dollars though, are we?

Mr. Stewart. No.

Chairman LaFalce. And so what would the total base be that you would be using?

Mr. Johnson. If you can get 100 to 200 awards, that is about 4 per State. That is enough to get people——

Chairman LaFalce. 200 times $25,000 is $5 million, right?

Mr. Johnson. Right.

Chairman LaFalce. So how much is being spent by the Federal Government right now for argument purposes? And would it be $5 million of the total amount being spent or do we have to get a percentage of every agency's marketing budget? I am thinking politically, too, it took us almost 4 years to get our SBIR Program through because we had to fight off virtually every agency and committee.

Mr. Johnson. Remember that the SBIR Program started with just one agency, the National Science Foundation.

Chairman LaFalce. I understand that.

Mr. Johnson. Then it grew to Defense. You could start with just the Department of Commerce and take all the money that they are presently spending on trade development, foreign commercial service, and do a set aside within the Department of Commerce.

Chairman LaFalce. How about a set aside within the SBA's very limited market for that purpose?

Mr. Johnson. They do not have any money to work with.

Chairman LaFalce. I know. That is almost nonexistent.

Mr. Little. I tried to make it very easy, in my recommendations, to go with what exists now because it is all set up. And again, it is not new resources. We are taking a few bucks out of Lockheed's pot and Douglas and these guys, and putting it into technology products.

It is my experience when you have a leadership technology position, the world finds you. They really do. I have equipment in Outer Mongolia. So, if you have the product and you have any kind of recognition in the United States in trade journals, they will come from all over; India, Pakistan, Russia, and so forth. So that is what is the key to getting us overseas. Better products with more technology.

Mr. Stewart. But that does not help the companies that are not run by Roger Little. Roger, let us be candid. We have a lot of them.

We have a lot of companies that can compete and can use as a basis of competition the adequacy of their product, prices, a lot of other things, and need help in other areas.

So, I do not think we ought to put the whole burden on technology to do the whole job. I think the Federal Government should do something in this area. I cannot help you right this minute with what account should this be hooked to. I come back, however, to tell you these are areas the States are and will spend more money in. And they are closer to small business, believe me, than even the SBA. And they are better able to work out a matching program with the States.

Chairman LAFALCE. If you use the SBDC, you have it.

Mr. STEWART. Sure. And give them a piece of some Federal account and say, to use it you have to come up with a matching grant of *x* or *y* or *z*. The SBDC has worked in the same limited way. This is a limited program.

If Commerce will go for it and if the Secretary will really support it, use them. That to me is the touchstone. Will he really fight for the money with OMB? Will he get the President's support? I believe both of these steps will generate great support in the country. We need somebody to really speak for them strongly. I think the troops are there, I really do. More than they have ever been.

Chairman LAFALCE. Fred, within the USTR, within the Department of Commerce, and within Treasury, do they have any concept of the special needs that the small business community would have? Or is this something, when you talk about small business and those agencies, they say we only have a little political constituency out there so periodically we have to appease them? Do you have a feel for it?

Mr. BERGSTEN. I think it differs among the agencies. Treasury, where I had the most direct experience, really deals with macro economic policy, tax policy, the exchange rate. It does not deal too much with either big or small firms on a direct basis. So probably the answer there is not much.

USTR is a small outfit. They are mainly involved in broad policy negotiations. Probably not too much there either. Commerce is supposed to, Export-Import Bank is supposed to. In my more limited direct experience with them I do not see as much concern expressed as ought to be to mobilize this kind of effort that I am talking about.

In my several experiences in Government, trying to work on expanding exports and improving our international awareness, I always felt it was a great unmobilized resource. And the Government really did not try hard enough.

Mr. JOHNSON. I think you have to say that comes from the top. It comes from where the budget decisions are made. It comes from the administration. And I commend anything you can do to get their attention.

Chairman LAFALCE. The President's council right now is being chaired by a constituent of mine, the chairman of Eastman Kodak, Coiby Chandler. Does the Export Council have representation from the small business community? Does anybody know?

Mr. **Bergsten**. I met with them about 2 weeks ago and briefed them on a lot of these things. I think they do have a membership in small business.

Chairman **LaFalce**. Do they?

Mr. **Bergsten**. But whether they are devoting any of their recommendations in that direction, I do not know.

Chairman **LaFalce**. I was just curious about the membership in and of itself.

Mr. **Johnson**. I am not sure how many people were listening to the President's Export Council or to the District Export Councils. There are small business people on the District Export Council. Some of them are active. They are very much successful if they have a good chairman who will really go out and spend a lot of time on it and beat the bushes. But in terms of getting the attention of the administration, I do not think they have it. They do have small business people on the President's Export Council.

Chairman **LaFalce**. Mr. Johnson.

Mr. **Johnson**. Could I make, Mr. Chairman, just one more point on the question of the Department of International Trade and the White House Conference recommendation?

Labels are unfortunate in that they serve as a handle and people begin to judge the contents by the label on the outside. Recommendation number 5, which has been labeled as the White House Conference recommends the Department for International Trade, is a very unfortunate label. Because the key words in that recommendation are that the international trade crisis mandates a number of priority actions. The Cabinet level department unfortunately got listed first in that text.

But many State recommendations folded or clustered their recommendations under that and got lost. And I hope that in your review of the White House Conference report you will read the fine print because the label was a very unfortunate one to describe what the White House Conference was trying to say on the need for better information, better coordinated information, better representation at GATT, better representation of small business throughout this Government in this international arena.

There is a lot there and the label is a misleading one.

The international trade department is not the key part of what people were trying to say. They were trying to say that this Government must give more attention and coordinate its efforts internationally. How they said that got buried this way.

Chairman **LaFalce**. I was not going to ask another question. But how did we jump then from no interest in 1980 to such great interest in 1986?

Mr. **Johnson**. A group of us were very concerned that the national issues, the 18 national issues that were picked out of the State conventions did not include one international issue. We met on Sunday night——

Chairman **LaFalce**. Since none of the 18 selected it, it has to be good.

Mr. **Johnson**. The White House Conference staff went through all of the recommendations and pulled out those that had 40 percent or more of the States covering or representing that issue.

Those were labeled national issues. There was not one international. We felt that they were discriminating against us.

Chairman LaFalce. In other words, it is not what the 18 State and regional conferences do. It is what you do the night before.

Mr. Johnson. Quite seriously, I would have loved to have been on the economic policy task force and I would have loved to have been on the innovation task force. But because I had a critical issue to work for, I spent my whole time in the international section. But people in the international section were all there because they were knowledgeable and very concerned at the lack of attention to the international side.

We went back to our State delegations and got agreement that they would vote for at least one recommendation. And this is the one we agreed to vote for.

Mr. Bergsten. Mr. Chairman, I was involved in neither of those White House Conferences. But I will offer you an explanation of why it changed.

Chairman LaFalce. Fred, you can always rise to the occasion.

Mr. Bergsten. Because I am a great believer in the importance of objective circumstances. In 1980 the United States had a current account surplus. In 1986 we had a deficit of $150 billion. Case rests.

Mr. Stewart. You have to know, Mr. Chairman, that while small business people may not be interested in exporting for their own companies, they live in the same towns and cities as you and I do. They see plants close. They see them go abroad. They are affected adversely by out sourcing. And between 1980 and 1986, Mr. Bergsten is exactly right. There was a change in the economy and small business knows it. But it is not prepared itself to put itself on the line about it until it understands and believes that the Federal Government knows what it is doing with respect to international trade and small business.

And there has been no confidence in this at all. And that is something that has not changed.

Chairman LaFalce. Very good. With that, we let you have the first word, Mr. Stewart. And we will let you have the last word, too.

The Small Business Committee will adjourn until 1 p.m. tomorrow.

[Whereupon, at 3:25 p.m., the committee adjourned, to reconvene at 1 p.m., March 19, 1987.]

APPENDIX

Prepared Statement of C. Fred Bergsten, Director, Institute for International Economics

The Challenge for American Industry

The American economy must achieve export-led growth over the next five years. We ran a trade deficit of $150 billion (on a balance-of-payments basis) in 1986. We have become the largest debtor nation in the world, and will owe the world at least $500 billion before our deterioration could possibly level off--requiring net interest payments to foreigners of at least $25 billion annually by 1990. Our oil import bill will almost certainly rise considerably by the end of the decade, in volume terms (as domestic production continues to decline) and prices perhaps rise further.

Hence the United States must improve its annual trade balance by something approximating $200 billion, even to restore balance--let alone the traditional, and probably appropriate, surplus--in our external economic position. A massive recession would "help" achieve this outcome by severely depressing imports, but is obviously an undesirable course. Hence the United States must launch a major export drive for at least the next five years.

Export-led growth is also essential for the overall health of the economy. Virtually all forecasts for 1987 and 1988 expect growth of 2-2 1/2 percent if an improved trade position contributes 1 percent or so a year. If the trade balance were to fail to improve, we would have a growth recession at best (with unemployment rising) and perhaps a true recession (with negative growth for at least two consecutive quarters). Continued expansion of the overall economy thus depends on export expansion, in addition to its critical role in balancing our international position over a longer period of time.

Moreover, American industry will over the next five years be unable to enjoy the rapid rise in domestic demand that has dominated its marketing strategies in the earlier 1980s. Domestic demand in our economy has grown by 3 1/2-4 percent per year even since the boom of 1983-84, providing a buoyant market for American producers (and foreign exporters). In the future, however, the growth of domestic demand will have to slow sharply--to 1-2 percent per year--to "make room" for domestic production to be exported. Hence American industry, including small business, must look increasingly abroad for markets to enable them to expand their production, create jobs and gain market share.

Can It Be Done?

Fortunately, the sharp decline of the dollar in the exchange markets over the past two years restores a good deal of international competitiveness to American industry. The dollar has fallen by a trade-weighted average of 35-40 percent against its major competitors in the industrial countries, and by even more against the Japanese yen and German DM. America priced itself out of world markets via the strong dollar during 1981-85, but is now back in business.

To be sure, further steps are needed to fully restore our export competitiveness. Economic growth in Europe and Japan is sluggish, and needs fiscal stimulus (mainly via tax cuts) to provide the dynamics needed to both sustain the world economy and provide markets for our trade improvement. The currencies of a few additional countries, notably Taiwan and Korea (to a much lesser degree), also need to rise against the dollar. The dollar may also need to fall further against the industrial countries' currencies, especially if their economic expansions do not accelerate. But American firms can compete again, and should lose no time attempting to do so.

Moreover, we can take comfort from the record of American trade performance in the period just before the strong dollar priced so much of our industry (and agriculture) out of world markets. From 1978 to 1980, American exports grew twice as fast as world trade. We regained global market share in every industrial sector and in every geographic market, in some cases back to the level of the 1960s. Our current account improved by over $50 billion in just those two years, excluding the adverse price effect of the second oil shock, and moved into surplus in 1980-81 despite the sharp rise in oil import costs.

We cannot be sure that a restoration of dollar equilibrium will enable us to regain the impressive trade performance of the late 1970s and very early 1980s. But the record of that period should be a source of confidence that we can do so. It should certainly give pause to those observers, both here and abroad, who doubt that America can still compete in the world. So should the annual rise of about 4 percent in productivity in our manufacturing sector since 1982, and the double-digit increase in real exports in both the third and fourth quarters of 1986.

What Should Be Done

A renewed American export boom, on anything like the scale which is essential for the health of the nation, will not just happen on its own. There will have to be a major marketing push by American industry to recapture markets abroad, especially in today's world where competition is extremely keen because growth is modest and inflation no longer hides industrial flaws.

Sucy a marketing push is particularly necessary because many American exporting firms became demoralized during the period of the overvalued dollar in the early 1980s and simply withdrew from, or sharply reduced, their international marketing efforts. These firms, which include some of our largest, face a reentry problem of substantial magnitude. They will have to redistribute resources to selling abroad, and make important corporate decisions to do so.

This problem is especially acute for small business in the United States. The vast bulk of our exports has always come from a handful of, mainly large, American companies. In general, small business has not been oriented abroad. Yet it will have to do so over the next few years for the reasons cited above. Hence the reentry and marketing problem must be of particular concern to American small business.

Most of the leadership to this end will have to come from the private sector itself. The government should do what it can to help, however, and should in fact make very effort to encourage a renewed export push by American industry--especially that part of American industry, small business, which has not heretofore been very active in foreign markets.

The most promising government instrument for playing such a role is probably the Export-Import Bank. Exim can both finance export efforts by American firms and make its expertise in foreign markets available to them, thus sharply enhancing their prospects for selling abroad. Through its small business program, Exim can be particularly helpful to the companies which are of concern to this Committee.

To carry out such a mandate, I believe that Congress should sharply expand the resources and mandate of the Export-Import Bank. The direct lending and guaranty authority of the Bank should be increased considerably. The Bank should be directed to use those resources aggressively to expand markets for American exports, including by matching the subsidy practices of foreign export credit agencies wherever those practices exist (via the new, hopefully expanded, "war chest" facility). The accounting treatment of Exim should be thoroughly reviewed so that only its real cost to the taxpayer, any subsidy element in its credit programs, is counted as a budget outlay. The Bank, working with the Department of Commerce, should lead the market reentry effort of American exporters.

Other policy steps can also be taken to enhance the export potential of American business, especially small business. But I would put major emphasis on expanding the programs of the Export-Import Bank, and recommend that the omnibus trade legislation of 1987 include a substantial component to that end.

Prepared Statement of James J. Harvey, Executive Director, National Commission on Jobs and Small Business

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Mr. Chairman . . . members of the Committee . . .

I am James Harvey, Executive Director of the National Commission on Jobs and Small Business. It is a privilege to appear before you today to discuss the Commission's final report, Making America Work Again: Jobs, Small Business, and the International Challenge. The report was presented to the 100th Congress on February 4.

At the outset, I want to express the Commission's appreciation for the exemplary support of the Chairman and Ranking Minority Member of this great committee, Mr. LaFalce and Mr. McDade. Your leadership and support, combined with 16 of your colleagues in the House and the Senate, made the Commission's efforts possible.

Although no Federal funds were used in the Commission's work, the support of 18 Congressional leaders underlined the policy significance of the Commission's agenda. Indeed, no public funds of any kind were employed by the Commission which was supported entirely by the private sector, principally by the Charles Stewart Mott Foundation of Michigan, supplemented by the Mellon, Rockefeller, Carnegie, and MacArthur foundations.

COMMISSION AND ITS CHARGE

By way of introduction, Mr. Chairman, I want to note that the Commission was created in September 1985, and requested to report back to the Congress in 15 months with recommendations to create 10 million jobs through small business.

I have had the opportunity of working with several bodies of this kind, but the energy of this commission was remarkable. The members contributed their time, talent, and experience generously to the Commission's work.

I understand that in the course of these hearings, you will hear from two members of the Commission, both also delegates to the White House Conference on Small Business: Milton Stewart, President of the Small Business High Technology Institute in Phoenix, Arizona, and John Rennie, President of Pacer Systems, Billerica, Massachusetts.

The Commission included, as well, leaders and executives from America's great corporations, financial institutions, universities, and scientific laboratories. Sam Beard, Chairman of the National Development Council, chaired the group on behalf of former presidents Ford and Carter who graced the Commission as honorary co-chairs.

The Commission was asked to examine several areas during its investigation:

- capital availability for small firms;
- international comparisons of small business development as well as export and trade issues related to small business;
- education, training, and retraining needs of the workforce and the small business community;
- technology and research and development;
- entrepreneurship; and
- the general economic environment for small business.

We carried out our Congressional mandate by scheduling eight hearings around the country on these issues, during which the Commission heard from nearly 100 witnesses and experts. The Commission also solicited papers from a variety of experts on economic matters, small business development, trade, and education.

COMMISSION REPORT

The result of this inquiry is Making America Work Again.

Mr. Chairman, three themes dominate this report. I want to review the overall report briefly before focusing on capital availability for small business and on the trade potential of small firms.

The first theme is international competition. As the report makes clear, we are living in a new age and a different world in which the United States has become an import sponge. Our inability to compete in world markets has created major difficulties for the entire economy: we are now the largest debtor nation in history; trade deficits have mushroomed; unemployment remains too high; we are losing world market shares across the board — in manufacturing, textiles, electronics, engines and turbines, even scientific instruments.

The second theme is an outgrowth of the first: our economy's capacity to support its people is in jeopardy. The ability of the American economy to continue to provide productive employment at attractive wages and salaries is increasingly in question. The evidence the Commission presents is disquieting: since 1980, we have lost over a million manufacturing jobs paying $25,000 a year, and replaced them with over five million jobs in service and retail establishments paying half that amount and less; real wages and salaries have been stagnant, if not declining, in the United States since 1972; average unemployment has increased by roughly two percent in each of the last three decades.

The third theme is that small business is an enormous asset to the United States in the increasingly competitive global economy, an asset that has until now been largely overlooked. Small firms account for about half of private non-farm employment in America; they produce 50 percent of the nation's gross domestic product; they are prodigious generators of new jobs, products, and innovations; and their capacity to turn on a dime to serve new markets is of enormous importance in the dynamic, fast-changing world around us.

What does all of this mean?

It means, as the report says, that for the first time in American history, our children's standard of living may not equal our own. The Commission's concern with this development is not simply materialistic.

Because the report also means that a fundamental aspect of America's idea of itself is in some trouble. As the Commission put it:

> "The American people need to be clear about the significance of the American promise. It represents far more than a platitude. At its core is our national affirmation of the dignity of the individual. The pledge that all can create their own destinies holds a powerful appeal to people around the world, and explains why generations of foreigners have sought a better future for themselves and their children on these shores. In offering all citizens the opportunity to pursue their hopes, the American dream is the source of social mobility in the United States and the foundation of our economic growth. That promise animates and sustains small businesss.
>
> "Now the legacy is itself imperiled."

It means that all of the enormous resources of the United States, including its educational system, its great corporations, its technological and scientific talents, its financial institutions and its small business community must come together in the economic competition the country faces. The Commission, for example, saw no gain for small firms in baiting large corporations — as the report says, restoring the fortunes of America's great corporations is a pressing national need and a crucial issue for many small businesses.

Finally, it means the country needs to take certain actions in order to reverse the drift into which we have fallen. The report cites five major areas in which we need to make progreess.

RECOMMENDATIONS

Let me review them briefly:

Mobilize Our People — Recommendation A called for leadership on the part of the public and private sectors to mobilize the American people to the realities of the new global competition around us.

Specifically, the Commission called on the President to make a major national address on competitiveness and employment; for governors to examine the effects of international competition within their states; for mayors and other local officials to foster a climate for small business growth and development; and for educators to do a better job preparing young people to compete in the modern world with emphasis on foreign languages and cultures as well as on entrepreneurial education.

Prepare Our Workforce — The report recommended improved educational efforts to provide workers and managers with the skills they need and to help the workforce develop the flexibility needed to adapt to new careers.

Specifically, recommendation B called for improved education at every level from preschool on, particularly in mathematics and science; it recommended much greater involvement of our colleges and universities with economic development; it urged continued business and government attention to training and retraining needs, as well as individual training accounts and portable pensions.

Mr. Chairman, I know that the next two areas of the Commission's recommendations are a particular focus of these hearings. Let me just cite the recommendations briefly here and expand on them later in this statement.

Invest in Our Future — The Commission's third recommendation was for doubling business investment in plant, equipment, and technology in the next five years. In addition, the report urged the development of new streams of capital for small business and for opportunities for more citizens to take a stake in the success of American business as equity holders.

Restore the "Yankee Trader" Tradition — Making America Work Again urges a United States policy of support for the fair trade of goods and services and the restoration of a vigorous exporting base that includes a large number of small firms.

Clear the Decks — Finally, the Commission recommended a series of steps that it thought would help business, government, and labor to become better organized to deal with the realities of international competition.

Recommendation E includes: reorganizing the Federal agencies concerned with trade and related matters, perhaps by establishing a Department of Trade, along with better Congressional oversight of issues related to competitiveness; the creation of a Congressionally-chartered Council on Competitiveness; a two-year budget cycle to improve the Congressional budget-making process; liability reform; small business impact statements on all tax legislation enacted in Congress; leadership on the part of the Small Business Administration in developing the credit systems and institutions needed by the small business community; and a White House Conference on labor management relations.

Mr. Chairman, let me review in some greater depth Recommendations C and D in the report, "Invest in Our Future" and "Restore the 'Yankee Trader' Tradition."

The Commission's recommendations in these areas were developed not in a vacuum but in the context of two detailed hearings on capital availability for small firms and on export opportunities. The first hearing was held at Federal Hall National Memorial on Wall Street, the site of George Washington's inaugural 200 years ago; the second was held at the Carter Center of Emory University.

INVEST IN OUR FUTURE

The Commission's report points to a number of impediments to productive capital investment that affect all firms. The impediments include low savings rates, the cost and use of capital, consumer debt, and what the report calls "the narrow base of capitalism."

These impediments create difficulties for all businesses, but particularly small firms. The report cites the following problems:

- Venture capital is available only for the cream of the entrepreneurial crop.
- Long-term financing for small business, i.e., funds for 60 months or longer, is almost totally unavailable.
- The dynamics of the financial community amount to almost an institutional prejudice against long-term investment in small business. These dynamics include misunderstanding small business, difficulties administering a loan portfolio with many small loans, prohibitions against financial institutions holding equity positions in business, and the lack of a well-developed secondary market to warehouse, market, and recycle small business loans.
- As the report makes clear, these problems are particularly acute in low-income and minority communities which lack the family savings essential to the initial financing of small business.

"It is impossible," says the Commission, "to avoid the conclusion that the capital needs of the small business owner have been largely ignored," a situation which must be corrected if we are to expect self-sustaining prosperity domestically.

The report urges encouraging savings, balancing the Federal budget, re-establishing the Investment Tax Credit, creating small business mutual funds as well as a greatly expanded small business loan secondary market, and the encouragement of long-term capital investment, particularly in small firms, through favorable treatment of capital gains. It recommended, as well, greater attention to research, development, and technology transfer by increasing the SBIR program to three percent of Federal R&D expenditures and the creation, in every state, of support systems for technology transfer that encourage partnerships between the academic and small business communities.

RESTORE THE "YANKEE TRADER" TRADITION

With respect to small business exporting, the Commission received the following evidence at the Carter Center hearing:

- Only ten percent of American firms export, and just 250 companies account for over 80 percent of the dollar volume of American exports.
- About 30,000 small American firms provide exportable goods and services but they export nothing at all because, in part, national and state efforts to identify and serve these firms are "notably deficient."
- Only one percent of the SBA loans were used for exporting between 1983 and 1986, and Eximbank, which finances the sale of American products abroad, has not used the full amount of loans and guarantees for small firms authorized by Congress.

Clearly we can do better. Clearly we must do better. According to the Department of Commerce every $1 billion in American exports supports nearly 25,000 domestic jobs.

Making America Work Again includes seven recommendations under the rubric of Restore the "Yankee Trader" Tradition. These are:

- Expand the General Agreement on Tariffs and Trade (GATT). The Commission recommended that the current round of GATT negotiations incorporate services and intellectual property rights under the provisions of GATT and that the GATT signatories consider some formula to recognize the economic burden the United States bears in supporting such a large portion of the defense costs of major trading partners.

- Import Quotas. The report urged a thorough review of existing American quotas and voluntary restraints that impede trade with an eye to removing those that can no longer be justified.
- Expand the Exporting Base. Recommendations include improving and simplifying the provisions for Foreign Sales Corporations to make them more useful to smaller firms, requiring Eximbank to market its small business export financing programs more aggressively, and creating a Small Business Exporting Incentive program similar in structure to the SBIR program.
- Serving Small Business. The report urges educating small business in exporting through aggressive efforts by the International Trade Administration to work with states and small business groups to disseminate information about programs available to small firms, reorienting ITA programs to focus on small business with evaluations tied to expanding the exporting base and not simply to the dollar value of exports; and actively assisting the formation of Export Trading Companies.
- Marketing Data. The Commission urges improving marketing data for small firms by developing an International Commerce Business Daily to provide timely marketing leads; encouraging large multinational firms to use small businesses as subcontractors and to provide market leads to American small firms; and establishing a public-private partnership to provide market analysis and information to the business community similar to the Japanese External Trade Organization.

o State Leadership. The report directed several recommendations at state officials. It recommended that each state should: (a) analyze its own trade flows with other nations; (b) establish promising exchange relationships with representative nations around the globe; and (c) sponsor small business exporting initiatives such as financing mechanisms, trade delegations abroad, state-sponsored Foreign Sales Corporations, and trade missions.

o A Conference on Summit Nations. Finally, the Commission stated that the summit nations should build on their statements that small business expansion is a key to non-inflationary economic growth by organizing a summit conference on small business and trade between 1990 and 1992. Such a conference could put small business owners around the world in touch with each other, encourage American businesses to learn how others are organized for world trade, and let others learn how small business has succeeded in the United States. It could also help educate the small business community in the complexities of developing policy for international trade.

If I could conclude, Mr. Chairman, I would observe that this Commission did not view the world through rose colored glasses. Although confident of our capacity to respond effectively, the Commission believed that unless we attend to the changed conditions of enterprise in the world, the long-term consequences for the United States will be quite severe.

"It is time," said the report, "that America came to its senses . . . . Because each generation of Americans has exceeded the standards of its parents in health, income, education, and material well-being, we have long taken our prosperity for granted. But now, a new prospect emerges: for the first time in recent history, our children's standard of living may not equal, much less exceed, our own."

But the United States is a vigorous and competitive country. Properly informed of the dimensions of the international challenge, Americans will respond effectively, just as they conquered the frontier, financed and prevailed in several global conflicts, and pushed back the boundaries of science and technology.

But in order to respond, we cannot delude ourselves with every conceivable excuse to explain the anemic economic performance of recent years. As the report states:

> ". . . our country has lost world market shares in good times and bad, on the back of a strong dollar and a weak one. We agree that the growth of services and information industries is significant and must be maintained, but we insist that an America stripped of its industrial and manufacturing foundation is inconceivable. The Commission has no desire to deny to the people of other lands the higher standards of living and material well-being their economic success deserves; but we are equally convinced their success does not require us to sacrifice the well-being of American workers and families."

Making America Work Again called on all Americans to join in this great competitive effort saying, "All will be tempered by it; none will be untouched by it; mastering it will be the making of our future."

Mr. Chairman, I am grateful for the opportunity to testify before the Committee, as well as for as for your leadership, and that of your colleagues, in providing a forum for discussing and acting on these important issues.

I have provided the Committee staff with several of the expert papers commissioned in the course of our work. I have also made available several of the press analyses, stories, and editorials that greeted Making America Work Again. I hope these materials can be included in the hearing record.

I will be pleased to answer any questions you may have.

ALTERNATIVE APPROACHES TO ENCOURAGING SMALL BUSINESS

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For National Commission on Jobs and Small Business

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ALTERNATIVE APPROACHES TO ENCOURAGING SMALL BUSINESS

I. Introduction

Small business is the mainstay of most industrial economies and essential to long term growth in developing countries. Businesses in this category can be differentiated by their product or service, their operations and their status in a particular country. Comparatively, these differences are extremely significant. Nonetheless, for those enterprises which actively engage in international trade, there are important similarities. These shared characteristics provide the basis for maximizing opportunities for small business through example.

The United States is exemplary in offering an economic climate conducive to the establishment and maintenance of small businesses. There are, however, bottlenecks which continue to exist and discourage businesses from entering directly into international transactions. Other countries, particularly those whose Gross National Product (GNP) have high export ratios, have developed effective approaches for this category of small businesses. No single country has yet written a blueprint for success but many have sponsored and hosted initiatives which could work well in the United States.

The range of options covers a wide spectrum. It would be limiting to consider only the obvious examples of government policies and programs in traditional trading nations. Newly industrialized and developing countries with the help of outside assistance have made important contributions in this area as well. Moreover, governments alone cannot underwrite the desired outcome of a prospering economy based on thriving small enterprise. Much depends upon the structure of the private sector and interaction of larger with smaller businesses. Governments can help foster these relationships but frequently, their interventions may actually have an unintended deterrent effect. Consequently, the choices available must include both government policies and programs and private sector initiatives, undertaken separately and jointly.

Empirical evidence suggests that where trade is involved, a friendly host environment for small business creation must include certain fundamental ingredients. Chief among them is access to capital and creative financing; either an effectively neutral tax policy for all industries at all levels or fiscal programs which offer a balanced array of incentives to small businesses; marketing and trade related assistance; and adequate horizontal and vertical collaboration between the private and public sector in a national economy. Alone, none of these elements can assure success. Together, the chances are much greater.

There are, however, certain basic imponderables. First and foremost is the level of entrepreneurship. Without this type of commercial dynamism no economic mix will be right to foster small business creation; second is the level of trade experience in a given economy. Equally important is the relative degree of vitality and competition in an economy. Small businesses cannot be willed or created in a vacuum. In the annals of small business lie too many stories of situations where the direct and hidden costs of doing business outweigh any program of incentives. Factors of production, particularly the cost of labor and capital, can serve as a tremendous disincentive to a new business entrant. Concentration, whether from government institutions or the private sector, is an obvious hindrance. By contrast small business thrives best under diverse economic conditions.

II. The Basic Parameters

2.1. *Finance*: Critical to any enterprise engaged in trade is the requisite financing needed to cover basic components of risk in an international transaction. In general, export financing as a ratio of corporate earnings is higher for smaller than larger businesses. As a result, the capital needs threshold for new exporters[1] is proportionately greater than it is for well-established operations.

Within this category every industrial country belonging to the International Monetary Fund (IMF) has special export financing programs. These cover direct loans, guarantees, diverse risk insurance programs, market development loans and coparticipation programs involving private banks and public financing organizations. Many of these countries offer trade-aid packaging programs which provide concessional financing directed at trade and investment in developing countries.

However, a majority of national programs do not make special allowances for small businesses. Instead, private and government programs are uniformly applied to all business applicants. Inevitably, large businesses account for the greatest share of these capital allocations, building in an inherent bias in favor of large, well-established firms. In recognition of this problem and the basic need to maintain a competitive environment through small business, a few governments and the European Community have instituted programs which offer a special window for new corporate entrants. Most of these programs are not new to the United States but a number of them offer alternate forms of creative financing.

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[1] Small business importers, other than trading intermediaries, are not covered in this report. Small firms characteristically rely on intermediaries or affiliates to cover their foreign procurement requirements. In those exceptional instances when the transaction is direct, the purpose remains primarily for input use and accordingly, is not considered directly relevent to small businesses whose principal activity is international trade.

On short and medium term export financing, Japan and France are examples of countries attempting to encourage trade participation by small and medium size businesses. Japan offers an array of programs which are described as a national strategy to convert small businesses from their primary economic role in the postwar period--acting as sole suppliers and holders of inventory for the large trading companies. Instead, the Japanese government has come to recognize, by its own admission, the dangers of a continuation of this relationship and is using trade and foreign investment financing to bring smaller businesses into the mainstream of international trade. The long-term strategy seemingly is to create incentives for these companies to transition out of traditional product lines and into higher technology products and services. The significance of these programs now would appear to be more a reflection of Japan's general industrial policy emphasizing high technology than a concerted effort to restructure the nation's economy in favor of small and medium-size businesses.

France offers a number of governmental programs, housed in their semi-autonomous insurance organization, COFACE, and its associate market research institution, ANVAR. The former works closely with private banks to develop prefinanced export financing as well as sales promotion and market development activities. Financing, both in French francs and especially foreign currencies, is rated extremely high by private industry and our own government.[2]

Equally notable are the favorable terms offered by COFACE. Comparing subsidy commitments on medium and long-term credits offered by the United States, France, Germany, Japan and the United Kingdom during the period 1981-1983 when a credit war among OECD countries was heating up[3] France had the highest interest rate subsidy.[4] In other words French funds were used to buy down interest rates to the benefit of all French exporters. National interest rates were high reflecting an intense inflationary period in France. To maintain their export competitiveness the French evidently were prepared to risk higher inflation through subsidized financing. Whether small business in France was helped in the long run as a result is difficult to determine at this time. Nonetheless, from the short-term standpoint, access to sufficient export financing and affordable risk insurance was secured for new entrants and well-established firms alike during this time period.

In agricultural commodities COFACE programs helped maintain the competitiveness of French exports, although not necessarily to the net gain of small businesses involved in this sector. Nonetheless, a comparison of COFACE program premiums for these agricultural exports with those in the United States for equivalent insurance programs and banking services points up a spread of at least 1.63 percent[5] in favor of lower French charges. *In other words the terms and effective rates for these programs may actually be more important than the substance of the programs themselves in servicing export and industrial policy objectives*.

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[2] Export-Import Bank. *Report to the U.S. Congress on Export Credit Competition and the Export-Import Bank of the United States*. September, 1984.

[3] The credit war became so intense as to inspire what is referred to as the OECD Consensus Minimum Interest Rates, supposedly an internationally determined minimum to be observed by all participating countries. The agreement was never enforceable but was observed by a majority of OECD members.

[4] All industrial countries have subsidized interest rates for small business enterprises in particular. See Appendix 2.

According to an Assessment Committee of The Economist Intelligence Unit reviewing small business incentives, Ireland and Greece rank the highest and Italy, Netherlands and the UK the lowest in subsidized loan capital.

Japan and France are equally illustrative of export oriented economies offering attractive and imaginative promotion and development programs. They include liberal financing for trade missions, scouting trips for development of affiliate or joint venture relationships abroad, trade fairs and the like. While the United States Department of Commerce sponsors trade fairs, which have proven very successful for business in general, European and Japanese financing of export promotion exhibits specifically make allowances for small business participation by offering generous financing and back-up services minimizing the cost to users, including small business.

Other types of export financing go relatively unnoticed by the finance community but in reality play an equally significant role. Forfeiting is one example. Whereas in the United States, buying and selling of notes collateralized on export contracts remains strictly the domain of private financial institutions, other countries such as Canada include this in the public sector mandate. Whether or not this is an advantage for small businesses is not certain, but the fact that *other trading nations approach the issue of trade and small business from a comprehensive, coordinated standpoint does provide an alternative approach to US programs*.

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[5] This calculation is based on an additon of insurance for ordinary, war, and guaranteed weight coverage and letters of credit--opening, irrevocable, and confirmation--and correspondent expenses plus financial charges for holding costs, etc. under COFACE and its US equivalent--GSM-102.

With regard to fixed asset financing at home and foreign investment there are numerous examples upon which to draw. Although not specifically directed at exports, this phase of capital assistance is the prerequisite to the establishment of any small business, including those which are trade oriented. Lacking well-developed private institutions for venture capital which has served small business so well in the United States, other countries have relied to a greater extent on government sponsored or collaborative programs where government funds and financial instruments are channelled through private banking institutions.

The European Investment Bank (EIB) of the European Community (EC), funds infrastructure projects directly in member countries and through intermediary institutions. In 1985, according to the Bank's annual report, forty-two intermediary institutions received ninety-six global loans,the largest share of which were concentrated in Italy. The loans are in a number of foreign currencies with repayments and interest payments in the currency of the loan. Although relatively large in scale because of the type of projects involved, the EIB does have a special program, the New Community Instrument (NCI), for small and medium -size companies in conjunction with its "global loan" program for priority investments explicitly involving small business participation.

Still another European institution, the European Coal and Steel Community (ECSC), provides subsidized interest rates on "reconversion" and "innovation" loans for small enterprises. Under these programs, when a financial intermediary in a member state extends capital for equity or training, the ECSC draws from its EC budget an equivalent amount of unsecured, subordinated NCI finance which would benefit, during the first period of the loan, from an interest moratorium charged to the general budget.

Aside from the attractiveness of the loan in terms of the below-market interest rate, another equally important feature is the reconversion/ innovation criteria for awarding such loans. The ECSC loan program is exemplary in that it recognizes the role small business can play in the structural economic adjustment. What is true for steel applies to other industries as well, particularly in manufacturing. EC reconversion loans take account of the dislocations created by trade measures, sometimes outside of any institutional control, and by changes in market conditions. The United States has traditionally left these types of adjustments more up to the market which has proven eminently successful for small steel manufacturers. However, in other sectors when the main vehicle for change depends solely upon the capital resources of venture capital, the adjustment which has a longer lead time may not offer sufficient return to warrant the attention of venture capital investors. In this case potentially efficient small businesses may be hurt more than large companies whose operations are in fact less efficient. Such companies are the most vulnerable to the shocks of trade-induced adjustments primarily because of their difficulties in accessing the requisite capital to ride out the conversion phase. Larger, more diversified firms with sufficient internal capital resources and credit lines stand a greater chance to turn the adjustment period to their advantage.

Trade/aid packaging is another area where the United States may lag behind some of its industrial competitors. Virtually all EC member countries individually and together, Japan, Canada and Australia have well-developed programs in this regard. The European Development Fund (EDF)[6] is the main arm of the EC's investment financing activities in developing countries[7]. A total of 80 percent of the fifth EDF was allocated in the form of non-repayable subsidies, 14 percent in the form of special terms (annual rate of interest of 1 percent over 40 years) and 6 percent in the form of risk capital (subordinate loans, conditional loans, loans to financial institutions). EDF does have a special window for small business, easing these firms' access to new markets through direct participation in technical assistance projects. There is an inherent trade component to this approach in terms of procurement for the project itself and longer-term income generating effects.

Similarly, the International Finance Corporation (IFC), the private sector affiliate of the World Bank, is the executing agency of new financial and management services for Caribbean and African countries[8]. These institutions are designed to encourage local small business enterprise. They also encourage and sponsor small businesses within donor countries through technical assitance project work and joint venture equity participation in those countries covered by these development facilities. The IFC has been criticized in the past for not having a sufficient share of small businesses in its investment portfolio. Although some investment projects in developing countries might qualify on employment or capitalization criteria as small business in industrial countries, they would be considered larger scale in the context of a developing country economy. Also, private sector equity in partial IFC-owned companies generally have been large-size multinational firms.

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[6] See page 22, in section 2.4 on Marketing Services.

[7] Most of these countries, referred to as ACP (African, Caribbean and Pacific countries), are associated with the EC under the five year Lome conventions. These conventions are the legal instruments for EDF allocations and funding arrangements.

[8] The Caribbean Project Development Facility (CPDF) includes participation from the United Nations Development Program (UNDP) and the Inter-American Development Bank (IDB). The Africa Project Development Facility (APDF) includes the UNDP and the African Development Bank (ADB). Individual countries also provide cash contributions to both facilities.

The African and Caribbean facilities are designed to correct this imbalance, by acting as a catalyst for investment in small-scale enterprise. Both institutions are staffed with only a few people because their role, unlike the IFC itself, is to identify potential projects and outside financial sponsors from the private sector as well as the IFC. An "African Management Services Company" is also contemplated. If established this company would be run by the IFC much like a private investment house or merchant bank which provides financial management services for a fee.

However different these developing country economies are from the United States, the approach to trade and entrepreneurship has universal application. It is particularly important that American small businesses are made more conscious of opportunities which currently exist under US and international organization auspices in this regard. It is equally useful for our own government to evaluate such programs so as to more closely integrate programs to encourage small business with financing incentives for trade and investment.

2.2. Tax Incentives

Governments have frequently used tax incentives to encourage investment in the establishment or expansion of small businesses. Tax incentives are less commonly found in government export promotion programs, and when offered, are usually available to all businesses. Even when measures are not specifically targeted for small business, government tax policy can create conditions favorable to small business through measures favoring investment.

Japan offers significant tax relief for small business, including: income tax allowances for small proprietorships, partnerships and corporations with an income less than Y47 million; special relief on dividend taxation for family owned businesses, and special depreciation provisions for small firms to encourage them to modernize in response to foreign competition. Japan has singled out technology exports in an incentive program for small business that provides a 20-35% deduction on revenue from overseas sales of technology. This is in line with the Japanese government's desire to encourage small subcontractors to develop products independently of their large domestic customers. Despite the above tax incentives, small business has not been as significant a source of innovation in Japan as it has been in the United States. This can partly be explained by Japanese laws that inhibit the availability of venture capital. These include: high capital gains tax (40-60%), prohibition of the establishment of investment trusts and tough standards for over the counter trading.

With regard to export tax incentives, New Zealand's export incentive package illustrates the range of tax incentives that can be offered to stimulate exports. These include tax deductions based on foreign revenues, deductions on foreign marketing expenses, additional depreciation allowances and exemption of machinery used for production of export goods from sales tax. For small businesses, these types of export tax incentives are a secondary form of assistance, subordinate to marketing and financial assistance which permit entry into foreign markets. In fact, the tax environment in the foreign market may be of more importance than any incentives offered by home governments.

2.3. Research and Development (R&D)

Resources for R&D are not normally associated with the export business as it pertains to product development. Nonetheless, there are arrangements among firms which are either specifically designed to bring new products on stream for well-defined foreign markets or assist in this regard through export-oriented applied research.

There are numerous private sector strategies in this regard. Large firms may establish affiliate relationships for purposes of defraying research and development costs. Joint ventures frequently piggyback these two functions, bringing together large and small scale enterprises for a shared purpose. In this instance the small business may be the originator of the research and the multinational firm, the developer and marketer of the product. Japan's small business structure is built on this pyrammidal relationship whereby the larger trading companies can buy relatively cheaply into highly differentiated products developed by small business. (See appendix F)

Government programs in R&D are very often motivated to provide a technological base through import substitution or to bridge the transition before small industry can become competitive for export markets. Many countries have national markets which would be too small to justify expenditures on R&D without the promise of higher returns derived form export markets as well. Their national R&D programs bear many resemblances and ultimately facilitate the entry of new firms into the export business.

Japan has implemented two non-traditional programs within the last six years, as they noticed a need for new programs if the small business community was to remain competitive On the technology side, a Venture Enterprise Center was initiated in 1980 to foster small and medium enterprises with superior research and development abilities. Research and develpment expenses often made up the majority of their total costs and as a result these firms had difficulty in securinng loans due to their lack of collateral. The Center enables venture businesses to receive bank loans by giving payment guarantees to banks. On the information front, a Small Business Information Center was set up within the Japan Small Business Corporation in 1980. The purpose of the center was to provide easy access for small companies to obtain timely information on the latest industrial trends and technical developments.

The EC's ESPRIT program, an R&D program designed to produce new information technologies, is aggressively being promoted for small business. Under this program, the Community contributes up to 50% for R&D costs. Parties sharing in the cost of an R&D project will be authorized to make use of the results of any joint work on a project.

Ireland has a well developed program established in 1980 that provides comprehensive product identification, development and ancillary services for existing small firms and potential entrepreneurs. The program entitled "The Innovation Centre", specifically provides three services: (1)People or organizations who have ideas for new or improved products can have those ideas evaluated and processed in the Centre from the idea stage through the marketplace. (2)People looking for product ideas are offered access to a business opportunities bank. This bank comprises product ideas from worldwide sources, which are suitable for manufacture by small firms. (3)Individuals can purchase innovation modules, e.g.- market and technical research reports on specific products, the use of equipment, workshops and pilot production buildings. The aim of the Innovation Centre was to provide a one-stop-shop product development service for small industry.

2.4 Marketing Services

Unable to tap the resources of large marketing departments, small businesses are hindered in the international marketplace by limited access to market information and technical expertise in exporting. Government agencies, business associations and chambers of commerce have sought to overcome this gap by providing export counseling and training, and overseas sales opportunities for small businesses. In most countries, these export services are available to all exporters, but small business is often targeted as the most promising sector for export growth. In any case, since large companies have less need for these services, small businesses are often the primary recipients.

Three types of services are generally provided to small business: market information, export management advice and export opportunities. Small businesses are provided with market information regarding market and economic conditions, regulations, industrial standards, culture and language in foreign countries. Export management training develops small business expertise in dealing with problems specific to exporting, including compliance with customs procedures, and arranging transportation and financing, among others. Export opportunities are generated for small businesses in efforts to match buyers and sellers both through listings and by providing opportunities for small businessmen to make contact with foreign buyers (eg. trade fairs and missions).

Small business export services are organized at both the local and national level in most countries, with varying degrees of decentralization and overlap between services. At the local level, export services are often offered to small business as part of a package of counseling services which also includes small business management advice, among other services - performed by local business information centers. These local centers rely on information collected by national trade agencies, although they may develop their own sources of information and networks of overseas contacts depending on local needs. They may be sponsored by national governments, state governments or private sector business associations and chambers of commerce.

While government-sponsored services in many countries are similar to those operating in the United States, some private sector organizations in other countries suggest new ways of providing export services at the local level. For instance, major companies in the United Kingdom have established Business in the Community (BIC), a non-profit organization charged with setting up 230 local enterprise agencies. In Greece, small companies work together in local cooperatives for production of footwear and clothing for export. The Lombardy Industrial Association in Italy created a special agency for foreign trade, specifically targeted at addressing the needs of small businessmen.

In Germany, France and Italy, chambers of commerce play a much larger role than in the United States, since membership is compulsory and they are more directly involved in regulating business activity (eg. trade certification). Drawing on the expertise of their foreign offices, chambers of commerce are especially effective in establishing business-to-business contacts that have multiplier effects in stimulating small business exports. This may be as simple as introducing a small businessman to a foreign agent or distributor who can market his product and give advice on product development for the foreign market.

At the national level, foreign trade agencies play a lead role in providing small business export services. For example, in France, the Center for Foreign Trade (CFCE) undertakes market studies for small and medium-sized firms, for which the government underwrites 50% of the cost. The program has produced results for small exporters, since 10% of the businesses receiving the studies have been able to write off the costs from increased business within a year, and another 40% have required extension of the contract for a second year to complete the write-off.

Organizing trade missions is a common function of national trade agencies, but the CFCE has provided increased incentives for small companies to participate in trade missions by financing 50% of the costs of the mission (including transportation, hotel and interpreting costs), repayable two years later following successful exporting to the country targeted by the trade mission.

The Scottish Development Agency is an interesting hybrid that acts as a catalyst to business activity by working closely with business and government. In partnership with small business, the Scottish Development Agency has developed innovative approaches to international marketing for small business. In one instance, the Agency funded an investigation into possible sub-contract opportunities in the United States Aerospace and Defense industries. The project also involved the identification of suitable work, assistance to companies to sell their capabilities in the U.S. market and the acquisition and monitoring of bid packages on behalf of the four companies hoping to target the U.S. market. The program is jointly funded between the Agency and the companies involved.

The Scottish Development Agency also used an in-store promotion to promote Scottish products overseas. A transportable "Scottish Village," with village green and pub, was installed at one of Tokyo's leading department stores to display a wide variety of retail produce from knitwear to confectionary. Sales on the first day exceeded any single day's sales in the entire store's 300 year history.

A West German non-profit service organization aimed primarily at small and medium-sized businesses is dedicated to improving the international competitiveness of West German business. RKW (Rationalisierungs-Kuratorium der Deutschen Wirtschaft) focuses on export conferences as a means of training small businessmen in international marketing. In one year, special working parties looked at Italian, Saudi Arabian and ASEAN markets. Participants benefited from short lectures by experienced experts from companies, consulting firms, chambers of commerce and industry, and organizations involved in export promotion, from the opportunity to exchange experiences with experts, and from the contact and information clearing house set up for the participants.

European Community (EC) export services for small business are a special case since the Ec is commited to integrating the internal European market by encouraging trade among member-states. The advantages gained through intra-EC trade - trading experience and cost benefits generated by joint ventures based on comparative advantage - may serve as a spring board from which small companies can export to other markets. This will depend on the success of EC programs in breaking down intra-EC barriers to trade.

Two EC programs are of special interest to small European businesses interested in exporting. The EC Business Cooperation Centre acts a sort of "marriage bureau" for small Community businesses by encouraging joint ventures between compatible firms. In another program, European Economic Interest Groupings engage in common cross-frontier services by taking advantage of an independent legal status that allows them to by-pass the variety of legal systems in the Community. The EC has also sought to foster transnational technology transfer by promoting exchanges between technology and management advisory services to small business.

Other EC policies designed to sharpen small businesses' competitive edge in the international marketplace are computerized market information and study grants for European industrialists. Through its Euro-net and Diane information systems, small businesses have access to information banks providing macro-economic and market data, trade contacts and sales opportunities (Japan has similarly sophisticated information systems). The EC also provides grants for young European industrialists to study in Japan, in order to develop greater understanding of the Japanese market and to promote exports to Japan.

The European Community encourages small business participation in contracts generated by aid programs in developing countries. As discussed in the Finance section above, market opportunities exist for European products and services as a result of European Development Fund Assistance to ACP countries and funding provided under Financial Protocols. Penetration of foreign markets via government contracts in developing countries may lead to additional export opportunities as small business exporters develop experience and contacts in developing country markets.

III. Deciphering a Model

In this review of export related programs for small business, the main point which emerges is that a healthy economic environment conducive to the establishment and success of small businesses is a prerequisite for effective government intervention in promoting small business exports. In the absence of a healthy economic environment, which is more a function of private sector activities and market forces than government interventions, no single program can ensure expansion of small business exports, no matter what the incentives. Several examples cited of national incentive programs certainly were supportive of small and medium-size enterprises in general and theoretically facilitated their involvement in international transactions. Existing data, however, is inconclusive respecting actual results. There is insufficient evidence to determine whether small firms owe their existence or their profitability to incentive programs. On the contrary, much of the literature indicates that those countries with the most forceful small business programs ranked lowest in the relative importance of these enterprises to the total economy.

Japan is a case in point. Throughout this report Japan ranks consistently high in terms of programs and institutional services on behalf of small business. However, the role of these companies in the Japanese economy has been criticized by a number of observers and by practitioners working in Japan. The main dilemma with regard to Japan is discerning whether or not small business is circumscribed in terms of growth by the high degree of concentration further upstream in the economy. With such a top heavy structure small businesses may be reduced to being contract suppliers of large industry, absorbing a portion of the latter's losses without appreciating any of the correspondent net gains.

Many European countries share the same problem. In the absence of venture capital many of these countries have opted for industrial targeting programs in favor of certain sectors involving small business. Trade is generally part of this paradigm. However, these same countries often are faced with the fact that small industries contribute relatively less to the economy than is true for the United States. There may actually be more economic concentration among those countries with the most comprehensive small business programs, which these programs are designed to correct.

Certain findings, however, emerge suggesting that a model for encouraging small business in exports must contain a number of basic factors in the context of a vital, open economy:

1) Export financing on favorable terms is essential given the difficulties experienced by small businesses in accessing sufficient capital to cover their requirements. Credit for operational costs and fixed assets is equally important but not directly tied to export development.

Government participation to subsidize interest rates can be helpful but it would appear that the greater the use of private intermediaries to channel funds, the more effective the programs. Creative financing by the private sector in the United States is virtually unrivaled but could be improved by comparison to other countries with regard to trade and foreign investment activities involving small business.

2) Government programs tend to be most effective when they entail a collaborative effort with the private sector. Joint venture arrangements on a private to private basis also are extremely responsive to individual firm requirements. Semi-government/private programs like the German chamber of commerce system also have proven successful, servicing small business needs to a greater extent than their large scale counterparts without being discriminatory. Obligatory membership for all businesses guarantees uniform

opportuntity while at the same time helping to underwrite a system whose services are of immediate application mainly for small businesses.

3) Decentralized programs often prove to be the most responsive to local business requirements. Centrally run programs run the risk of being less sensitive to such important considerations as local labor and market conditions and existing business relationships. The Scottish program is an illustration of an integrated approach which is sensitive to local production factors without being overloaded with administrative features.

Numerous small business surveys conducted in the United States reach similar conclusions that paper work is one of the biggest obstacles to participation in government programs. Another consideration is the cost of any program which is top heavy in terms of administrative procedures. Not only can such programs be a deterrent to assisting small business but they are inherently cost ineffective. The larger the outlay for administrative duties, the higher the indirect cost to program recipients themselves.

4)Service programs have a high multiplier effect for small business, particularly with respect to trade. Surveys of American businesses point out that the lower level of business involvement in trade either for manufactured products or services stems in part from uncertainties involving international business. To the extent that activities like training programs,international trade shows, and reciprocal distribution arrangements for example can reduce the psychological barriers to trade, the more effective will be other programs and activities designed to promote small business involvement in trade.

5) European programs which service trade on an intra-EC member country basis more closely resemble international trade than interstate commerce in the United States. As a result, there is a built-in international trade dimension to many of the small business programs in Europe which is difficult to replicate in the United States. Government programs which encourage joint ventures with multinational firms may offer comparable benefits to American small business which intra-EC member marketing offers European firms.

IV. Recommendations

American programs, notwithstanding their high standard for small business in general, could be more effective in terms of trade generating operations. With this objective in mind, we recommend the following cost effective initiatives:

1) Creative trade financing in the private sector encouraged by government involvement along the lines of the Trade and Development Program in the Agency for International Development or Eximbank's small business and medium-term credit program. Consideration should also be given to a form of exchange rate stabilization insurance which insures against losses above a certain band attributable to widely fluctuating exchange rate.

2) Trade/aid packaging as a means of securing entry into new growth markets. Small businesses should be apprised of existing programs and be given priority in participating in technical assistance and procurement projects.

3) Greater collaboration between the private sector and government as well as within government itself in order to develop a concerted trade oriented program for small business.

4) Improvements in service related activities oriented to trade. Computerized information services accessible to small business users would be helpful, assuming the content was evaluated and trade oriented. Foreign business contacts or joint venture opportunities, for instance, are not very useful in the absence of some evaluation. Quality information is key.

5) Improvements in marketing assistance overseas and appropriate dissemination of this information at home.

6) Reductions in administrative costs and encouragement of decentralized programs. The Federal government should devote as much effort as possible in working with states and municipalities to reach local industry effectively.

ENCOURAGING U.S. EXPORTS BY SMALL- AND MEDIUM-SIZED FIRMS

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ENCOURAGING U.S. EXPORTS BY SMALL- AND MEDIUM-SIZED FIRMS

Export activities are important for the economic well-being of a nation. The arguments of specialization and comparative advantage notwithstanding, in the long run, a nation has to generate sufficient trade outflow to compensate for the inflow activities taking place. A deficit situation can only persist as long as "foreign countries are willing to accept the IOUs of the deficit country, and permit it to pile up liabilities." (1)

The United States is currently experiencing a chronic balance of payments deficit, triggered mainly by imbalances in its merchandise trade. In the past years, the trade deficit has grown continuously, reaching in 1985 a record high of $148.5 billion. For 1986, increases up to $170 billion are projected. Since there is growing concern about the future repercussions of the resultant U.S. international debt, it is important to arrest and reverse this trend.

Explanations for the existence of this huge and ever growing trade deficit have been manifold, and have blamed mainly the high volume of foreign oil imports and the high value of the dollar. While these macro factors, to be addressed later, certainly have played a role, it is also a fact that most U.S. firms, particularly the small- and medium-sized ones, lack an export orientation. Estimates by the U.S. Department of Commerce indicate that "half of all U.S. exports of manufactured products are made by only 100 companies, and that 80 percent are made by 250 companies." (2) In hearings before a Congressional subcommittee, testimony indicated that about 20,000 U.S. firms are believed to be capable of exporting, but do not do so. (3)

Low U.S. participation in international trade is further evidenced by the comparatively low volume of our per capita exports. For example, if intra-Community exports are included, the EC exports $2,400 a year for every man, woman and child. The figure for Japan is $1,400; for the US, it is only $1,000. (4)

The lack of export performance by U.S. firms is explained in various ways. One of them is that the U.S. has historically been a closed economy and relatively independent of foreign trade. In the past, because of its size and the diversity of its resources, the American economy was able to satisfy consumer wants and national needs with a minimum of reliance on foreign trade. (5) The availability of a large U.S. domestic market and the relative distance to foreign markets resulted often, on the part of our firms, in an unfamiliarity with foreign markets. U.S. small manufacturers "have grown up in a market that, by its magnitude, has served very well to conceive and nurture its industrial children. Unlike manufacturers in most industrial countries, we have felt no compelling need to seek [business] beyond our national borders." (6) As a result, the perception on part of many businesses has emerged that "exporting is too risky and complicated, and not worth it." (7) Over time, many corporate managers have held the attitude that "exports are [a] marginal business," (8) and, due to the current onslaught of international competition within the U.S. market, have developed a fear of international market activities. Many firms tend to see only the risks -- "informational gaps, unfamiliar conditions in markets, complicated domestic and foreign trade regulations" (9) -- rather than the opportunities that the international market can present.

Overcoming this fear of international markets, and convincing our firms to become active players in world trade, is of crucial importance today. Clearly, the U.S. will not be able to continue, for the sake of its economic and national security, to accumulate growing trade deficits in the years to come. Attempting to achieve a deficit reduction through the restrictions of imports will ~~only~~ lead to a surge of worldwide protectionism, a substantial decline in the standard of living, and an undermining of the economic foundation of the free world. Other than in decades past, the encouragement of U.S. exports can no longer be a goal of convenience, but must rather become an objective of national priority.

THE RELEVANCE OF SMALLER-SIZED FIRMS TO U.S. EXPORT PERFORMANCE

In spite of only limited participation in exporting by small- and medium-sized firms, their involvement in the international market has become increasingly critical. Small- and medium-sized firms form the core of the U.S. economy. Over the past years, small- and medium-sized firms have consistently outpaced larger firms in terms of employment generation. These firms have also continuously been a fount of innovation and creativity, furthering the capacity for progress of the nation. Moreover, from the societal viewpoint, it is the small- and medium-sized firms which offer the potential of fulfilling the promise of the American Dream of entrepreneurship, and which are therefore a major foundation of our social structure. If these firms continue to be deprived of international business experience and are unable to hone their competitive skills abroad, they will lose out on state-of-the-art knowledge and will increasingly be exposed to the danger of being driven against the wall by foreign competition entering their home ground.

Another major reason which emphasizes the need for getting more small- and medium-sized firms involved in exporting is that of the corporate life cycle. Our current corporate giants will not necessarily stay on top forever. History has shown that large institutions are often confronted with crises and insurmountable difficulties, leading to their eventual decline. From a societal perspective, such a decline is acceptable, and can be healthy, as long as there are new firms preparing to assume the position of the corporate giants of tomorrow. Such a development is only possible, however, if systematic efforts are undertaken to groom the small companies of today for progress and for further growth. Given the size and importance of the global market, it is therefore imperative to encourage small- and medium-sized U.S. businesses to participate in that market, so that they can become the large corporations of the future.

Small- and medium-sized firms are not, as many believe, totally unequipped to enter international competition. On the contrary, their small size can provide them with major competitive advantages over large firms. For example, in a smaller-sized firm, the customer can benefit from shorter response times. If some special situation should arise, there is no need to wait for the "home office" to respond. Responses can be immediate, direct and predictable to the customer, therefore providing precisely those competitive ingredients which increase stability in a business relationship and reduce risk and costs.

Smaller-sized firms can also customize their operations more easily. In a large corporate system, any changes are often subject to delays as various layers of management are consulted, costs recalculated, and multiple communication levels exercised. In a smaller-sized operation, procedures can more easily be adopted to the special needs of the customer or to local requirements. Smaller firms can also offer clearer lines of accountability. Decision-making and accountability are often directly linked in a smaller firm. The decision-maker is more visible and responsive to the customer. If something does not go according to plan in a smaller-sized firm, the customer knows who to contact to fix the problem.

Smaller firms also are much better equipped to handle exceptions. For international sales situations which have high variability, either in terms of the timing or the nature of the sale, a smaller-sized firm can usually provide a more flexible framework for the decision process. Exceptions can be handled when they occur rather than after waiting for concurrence from other levels in the organization.

Finally, smaller firms offer to their customers better communication linkages. In large corporate structures, communication must often move through several layers of management before decisions are forthcoming. This can result in action delays and can complicate what might be a simple decision. In a smaller-sized firm, communication links are direct between the provider of a service or product and its user.

As a result, international operations by smaller firms can be more flexible and responsive than those by corporate giants. Therefore, there are reasonable prospects that the customer can obtain higher customer service levels with lower investments. Given the increasing demand in the international market for short term responsiveness, flexibility, adaptation, and high levels of service, small- and medium-sized businesses due to their structure, possess a unique advantage which can propel them successfully into the international marketing arena.

DIFFICULTIES FACED BY FIRMS IN THE INTERNATIONAL MARKET

The obstacles encountered by firms planning to enter or having already entered the international market, can be classified into micro and macro difficulties. Macro factors are those relating to what has been labeled the international playing field. Here, two major concerns are apparent: one deals with the existence of the playing field; the other, whether or not the available playing field is level.

Three conditions are necessary for the existence of an international market. These are: market demand, market access and market reach. Our firms encounter problems with all three of these. Lack of market demand is encountered since insufficient funds are available to customers abroad, be they individuals or institutions, to purchase foreign products. This is usually the result of a lack of foreign exchange funds. Market access difficulties, in turn, result from obstacles put into place by foreign governments in order to limit market entry and/or market performance by our firms. Market reach, finally, refers to the fact that, on occassion, our firms are not able to serve a particular foreign market with their products due to restrictions imposed on them by their own government. Such restrictions are primarily in the form of export controls imposed due to foreign policy, national security or short supply concerns.

These three types of problems hinder the export effort of all firms -- small, medium, and large alike. Yet the smaller firm is at a disadvantage when compared to its larger brethren since it can not seek recourse to options available to the corporate giants. For example, large companies will have much more clout in requesting government assistance to achieve the openings of markets. Similarly, large firms are better equipped to handle onerous government burdens such as export controls through their own in-house legal departments. This difference becomes even more pronounced when firms have been able to overcome these obstacles, and are subsequently faced with an international playing field which is not level.

Various factors contribute to situations which place U.S. firms at an unfair competitive disadvantage. These factors are summarized in Table 1. One major obstacle is the effect of exchange rates. In recent years, financial flows rather than trade flows are determining exchange rates. Governments have frequently taken recourse to manipulating exchange rates and have managed to create an environment which allows their own firms to offer low export prices, while making imports quite expensive. As a result, U.S. firms are placed in double jeopardy. They encounter great difficulties in marketing their products abroad and are being hurt in their home market by underpriced foreign products.

Our firms also frequently encounter unfair competition abroad because they are pitted against corporations which are subsidized by their governments. In addition, they meet increasing competition from state enterprises, whose profit calculations are entirely different from those of a firm which has to survive in a free market environment. Foreign governments also offer preferential treatment to their firms, making it much more difficult for U.S. firms not benefitting from such preferences to compete. Other factors which distort the international competitive situation are differences in tax policies, anti-trust statutes, and domestic regulations. These measures, which are often implemented with strictly domestic economic policy concerns in mind, can frequently have major repercussions on the international trade performance of our firms.

Again, all of these impediments to international trade affect both large and smaller-sized firms. Yet, in most instances, large multinational corporations ~~can~~ avail themselves to more options in terms of location, the shifting of funds, and the obtaining of subsidies abroad. Small- and medium-sized firms do not have these alternatives. The only area where at this time small- and medium-sized firms are in a more advantageous position than their larger counter-parts, is that of anti-trust. Due to the Export Trading Company Act of 1982, small- and medium-sized firms have greater flexibility in forming cooperative arrangements with the goal of penetrating foreign markets.

After having found a foreign market, and having developed ways to deal with obstacles of unfair competition, our firms are still not yet fully able to participate in export activities. As a series of surveys conducted since 1979 by the National Center for Export-Import Studies at Georgetown University has shown, small- and medium-sized firms encounter a substantial amount of export transaction problems. These problems (listed in Table 2) are often major ones, which prevent smaller-sized firms from entering international markets. They cover operational, marketing, and strategic concerns, and are the results of shortages of resources, expertise, and desire. Some companies, for example, are concerned about how to package and transport a product, and how to ensure that they will get paid for an export. Some are worried about finding foreign customers, and delivering an effective sales presentation. Others encounter major difficulties in supplying the follow-up service which they need to deliver in order to sustain an export relationship. Although some of these problems may seem petty, they represent the major internal reasons why small- and medium-sized firms in the U.S. do not participate more in international markets. Restructuring the global market environment alone will be insufficient to get these firms to become more active participants in global marketing. Only when these export transaction concerns are addressed to the degree that firms feel comfortable in handling them, will our companies consider international marketing as a strategic alternative. What considerations, then, must be kept in mind in the design and implementation of programs which encourage the export effort of small- and medium-sized U.S. firms?

DESIGNING EXPORT ASSISTANCE PROGRAMS

Currently, the U.S. government provides export assistance in a variety of ways. Information is made available to firms, emanating usually from the U.S. Department of Commerce, and compiled with the assistance of foreign commercial service outposts abroad. Manuals and brochures provide general information on market potential or on economic developments abroad, and offer listings of potential dealers and distributors. In addition, information is provided on specific foreign firms by supplying financial and commercial data and naming sources for credit information.

A second major thrust of export assistance consists of financial incentives. Tax-based incentives such as the Foreign Sales Corporation mechanism (FSC) aid firms by sheltering foreign income from taxation. Export financing incentives are provided by the Export-Import Bank of the United States (Exim Bank). Such financing enables U.S. firms to enter transactions which require large and sometimes low-cost loans, or to decrease their risk through insurance of credit extended to foreign firms.

A third major approach used by the U.S. government consists of environmental facilitation. Governmental efforts serve to address macro problems of trade by conducting trade negotiations, bilaterally and multilaterally, in order to facilitate the export flows from the U.S. Government agencies also organize, encourage, and sponsor trade shows, trade missions and trade exhibits abroad. In addition, catalog shows and in-store promotions are conducted abroad, sponsored or co-sponsored by the government. Also, foreign buyers who are visiting the U.S. are frequently routed to U.S. firms.

Despite the existence of a myriad of programs to facilitate U.S. exports, however, the impact of these programs appears to be insufficient. Our trade deficit keeps rising, and most of our small- and medium-sized firms are still not involved to any meaningful extent in international trade. Insufficient market response, along with research findings that small- and medium-sized firms believe that the helpfulness of governmental export promotion programs actually decreases with increasing export experience (10), points toward the need to restructure our current export promotion efforts.

RECASTING EXPORT PROMOTION PROGRAMS

In order to make our export assistance more effective and efficient, our current efforts need to be restructured, and new efforts need to be undertaken. The restructuring of current efforts needs to consist of four crucial steps: a return to basic objectives, a segmenting of firms, a focus on the foreign buyer, and a redefinition of the terms of access.

Return to Basic Objectives

Whenever we design a trade promotion program, we go about it in a very straightforward manner. Since we want to help firms export, we go to companies and ask them about the type of help they desire. These firms then provide their responses in surveys or interviews, and, based on these answers, we then put a program in place that responds to the requests. Later on, we often discover that the programs initiated do not have the expected effect on export performance.

This occurs because this is a fundamentally flawed approach. We need to remember the initial objective, which is not to simply go out and help firms, but rather to help companies improve their export performance, and, via such an improvement, to increase the number of jobs. By just asking our firms what help they want, governmental programs often become active in areas that are of specious value. For example, if we ask firms whether or not they would like better information on foreign markets, they will undoubtedly answer "yes." Similarly, if we ask them if they would like better export financing conditions, again they will agree. In all these instances, we are taking the "motherhood and apple pie" approach. Of course everybody is for programs that enhance profitability and make life easier. However, the real question is whether or not these programs will result in more exports. This crucial link between the program and improved export performances is often missing.

For example, subsidized export credits will not necessarily enhance export performance. In some situations, subsidized credits may be necessary to counteract foreign practices. But if financial assistance is provided without such necessity, the subsidization may only result in improving the profitability of a domestic firm for transactions that would have taken place anyhow, or it may mean that we are forcing our trading partners to offer similar preferential rates. In such instances, of course, all we are doing is making our goods available at better conditions to foreign customers, while not improving our sales performance.

Similarly, an increase in information flows, whether on foreign markets, foreign customers, or foreign business practices, even if desired by firms, may be useless if it only results in the production and mailing of more tons of paper. An increase in the quantity of information will not necessarily mean that business will absorb and use the knowledge. Specificity, accuracy and timeliness of information play a much more important role than volume. Information flows should not focus on information per se, but only on the type of information that will enable our firms to perform their foreign sales activities better.

It therefore becomes imperative to structure any export assistance program with the basic objective of export sales improvement in mind. Before continuing old programs or implementing new ones, a definite linkage between program usage and export performance needs to be drawn, and these linkages need to be continously monitored for their effectiveness.

Segmenting Firms

It would be unreasonable to assume that all exporters have the same needs. Yet, most export assistance programs are developed with a shotgun approach - trying to offer everything to everybody. Not only does such an approach result in a waste of resources, it also reduces the effectiveness of export assistance. For example, firms, which have to wade through huge volumes of materials in search of the one piece of information in which they are interested, are likely to be either discouraged by such a task, or will disregard the information entirely. A viable export assistance program needs to offer help which is targeted as closely as possible at the specific area where a firm needs help.

Research has shown that firms can be differentiated into segments according to their level of international experience and activities. Various theoretical and empirical studies have identified such segments first in a general fashion (11,12), and gradually in a more refined form (13,14). Table 3 shows such a possible segmentation scheme. By differentiating firms into different categories based on their export experience, export assistance programs can target the needs of firms, and respond precisely by providing assistance in those areas where firms need help most. For example, firms with only a beginning interest in international marketing may need help primarily with the financing of exports. More experienced exporters, in turn, may need help most in establishing better distribution networks abroad.

Any export assistance program, be it at the national or regional level should therefore start out by gathering information about the firms that are to be served, and then classifying them by the international stages of their experience. Subsequently, the export assistance needs of the firms in each stage need to be determined.

Programs should then be developed which satisfy the needs of each group by aiming at the individual segment of firms rather than at the total economy. This way, users of such programs will be more satisfied, and resources will be expended more wisely. An example of such a differentiated approach to export assistance planning is provided in the appendix of this report.

Focus on the Foreign Buyer

Export assistance programs also need to incorporate, as a fundamental concern, the needs and desires of the foreign buyers of U.S. products. In terms of export performance, it must be remembered that the U.S. firm is only an intermediary. A successful sale is dependent on the foreign buyer. Any viable assistance program should therefore find out what needs to be done to make our products more desirable for purchase abroad. In the development of an export assistance program one needs to spend time and effort to obtain more information about foreign buyers. One needs to conduct surveys abroad among former, current, and potential buyers of U.S. products. One needs to find out where these foreign buyers see the benefits and drawbacks of purchasing U.S. products.

Such an exploration of foreign buyer behavior must also include trade off considerations. For example, it is insufficient to simply state that price competitiveness is all that counts. An international transaction rarely consists of price considerations alone. Any export assistance program needs to find out from the foreign buyer what it is our firms can do in order to regain their overall international competitiveness. This may mean that our firms have to concentrate on offering better product quality, better service delivery, better communications with foreign customers, or shorter delivery times and quicker responses to orders. But only if we have a basic understanding of these buyer needs, can an export assistance program take measures to enhance the desirability and therefore the appeal of U.S. products abroad. (15)

Redefinition of Terms of Access

Currently, export assistance programs, particularly in the macro sector, aim to obtain market access for U.S. products. As a result, lengthy negotiations are held with those trading partners who enjoy large trade surpluses with us, encouraging them to purchase more U.S. products. If sufficient pressure is applied, gradually the purchase of these products will increase on a sectoral basis. Such an approach is, however, insufficient. It treats our trade deficit as the problem rather than the symptom. It will result only in temporary improvements in our trade posture, and will leave U.S. trade performance at the mercy of foreign governments, who can turn off trade flows just as easily as they have turned them on. Our trade enhancement programs need to redefine the goal of market access. Rather than battling for market access for our products, our trade negotiators need to aim for market access for our firms. Only when our firms are able to enter foreign markets, learn the business customs, establish business ties, and integrate themselves into the foreign economy, will their international trade effort truly become entrenched. It is our companies as much as our products which need a firm foothold in markets abroad in order to turn our long-term trade performance around.

DELIVERING EXPORT ASSISTANCE

Aiding our small- and medium-sized firms in improving their export performance requires steps at both the national and the international level. Internationally, we must ensure that there continues to exist a playing field for our firms, that this playing field will be as level as possible, and that there are rules which are known and to which everyone adheres. This requires major international steps to be undertaken to stimulate market demand abroad, to enable the indebted countries to restore their economies, and to again offer market opportunities to our firms. It also requires a harmonization of monetary and economic policies, so that firms are not taken aback by wide exchange rate fluctuations and economic changes which cannot possibly be predicted or absorbed. It must be the role of government to restore an economic climate which to some degree is predictable and consistent. In addition, government must identify unfair trade practices early on and move quickly to negotiate their removal. Alternatively, retaliatory measures must be swift, massive, and harsh. While, as a national posture, we should continue our policy of open markets, we cannot do so at the expense of de-industrialization at home.

Export assistance also needs to come about through a changed national orientation towards trade. U.S. firms need the assistance of the public sector in order to compete successfully abroad. "A boom in U.S. exports cannot be achieved by the private sector alone, because export weakness has stemmed at least as much from public policy as it has from private initiative." (16) What is needed is more than just another export drive. Longstanding and deeply ingrained policy stances need to be reversed. The interdependence between the U.S. economy and the "rest of the world" needs to be recognized and acted upon. Policy thinking at all echelons of our government needs to be permeated by considerations of international trade repercussions. Export trade considerations need to become an integral part of our domestic policy posture, encouraged perhaps by the development of an "export impact statement" for each major legislative or regulatory decision.

Whenever we change our liability laws, look at our anti-trust legislation, or create mechanisms such as the superfund, we need to recognize that there will be implications of these steps for the international trade performance of our firms. (17) While we cannot, and should not, expect government policy to be oriented on international business concerns alone, there should be at least a national posture which provides a benevolent environment for the international trade effort of our firms.

As far as specific export assistance programs are concerned, we need to carefully scrutinize and evaluate them as to their effectiveness. It is difficult to advocate a broadbrush increase in activity and funding for export promotion at a time when there is a national effort to reduce governmental expenditures. Moreover, export marketing assistance research has so far not been able to conclusively show that export services and programs have had any impact on the management and performance of a firm or an economy. (18, 19) We need to carefully evaluate the areas in which government should be involved. Many areas which are admittedly in need of improvement in order to foster the export efforts of our firms are best left to the private sector rather than to governmental intervention.

Governmental efforts should concentrate exclusively on the closing of market gaps. This does not mean the provision of artificial export profitability or the procurement of artificial market access. It also does not mean that government programs should direct firms on how to adapt their products or how to change their manufacturing processes. (20) Rather, it refers to government involvement in areas where, due to financial requirements and considerations of power, time, or resource commitment, the private sector has been unable to perform a necessary function.

A primary area for government involvement is in the field of information collection. It will be difficult for the private sector to build, without any government support, an information flow network which can provide accurate, timely and detailed responses to the international marketing questions of firms. Given the data collection activities already in place within the government, it seems appropriate to maintain and strengthen these efforts. However, the subsequent distribution of such information could very well become a private sector activity.

Similarly, there is a clear role for government to fill market financing gaps. These gaps exist in instances where the size of a project, the length of time necessary for its completion, the risks associated with it, or the dearth of information on it, present insurmountable obstacles for the private sector. In such cases government involvement is appropriate and necessary.

Direct governmental assistance can also be extremely useful when it comes to the opening of doors. A trade mission headed by a high-level government official can often, for reasons of protocol, obtain much better access to other governments or high-level executives abroad than a private sector venture. Embassy support abroad can help the visiting business executive by pointing out the major players, explaining the rules of local business and making introductions. A further strengthening of the U.S. Foreign and Commercial Service by using some old-fashioned incentives for entrepreneurship could be very helpful.

The public sector can also play a role by performing the function of catalyst -- i.e., by organizing activities without direct participation -- and by furthering the role of incubators which provide the necessary "critical mass" for our exporters. For example, many small U.S. firms are not exporting because they view the entry expense to the international market as too high. A firm may simply not have, or be willing to spend, the money to find out about foreign ~~sales~~ potential or to identify foreign distributors. Sometimes the investment in such activities cannot be justified if the initial return potential is low. This is particularly the case when initial market investment requirements are high and market penetration times are long.

In such situations, public sector export assistance efforts can make a crucial difference, if these activities can be performed less expensively -- due to economies of scale -- outside of the individual firm. In most instances, however, it would be sufficient to develop governmental facilitation of a private sector activity to bridge such a gap, rather than having the government perform such services directly.

In this context, perhaps another look at the Export Trading Company legislation is in order. Many see this legislation today as unsuccessful and not worthwhile to pursue. It appears, however, that this is a premature judgment. If one looks back at the original intent of the legislation -- to permit the development of one-stop shopping centers for foreign buyers, cooperative efforts among firms, and closer involvement in trade by banks -- we find this intent to still be valid and to have tremendous potential for improving our international trade activities. Thus far, the legislation simply has not been used in the right way. If export trading companies are created in sufficient numbers, provided with sufficiently strong protection against anti-trust procedures, and are given more flexibility in their operations, appropriate financing, and sufficient incubation time, they may yet emerge as a significant propellant for U.S. export efforts.

It should also be considered that, for small- and medium-sized firms, particularly those without any export experience, incubator assistance is crucial. No amount of literature will come even close to providing the assistance rendered by experienced peers who can help a firm initiate, negotiate and conclude an export transaction. Left to fend for themselves, firms are quite likely to abandon any export effort, since management is too preoccupied with the daily problems of doing business domestically. If the actual conduct of export transactions is demonstrated, and if the profitability of such transactions is experienced, these firms will be well on their way to continue their active participation in the international marketplace. Such incubator work must therefore be conducted by experienced exporters, who understand international transactions, and who can look back on an established export record. A public export assistance program can play a major role here. If the private sector is unable or unwilling to develop such incubator activities, public assistance could be used to raise the level of profitability of these efforts to the threshold of feasibility. Our small firms may need too much hand-holding to make it worthwhile for an experienced firm to offer export assistance. Yet, given some incentive based co-financing or tax measures, experienced exporters may very well be willing to undertake such an effort.

As to the question of who, within the public sector, should perform all these activities, a differentiated approach seems worthwhile. International negotiation efforts, macro policies and broad information gathering should most appropriately remain in the purview of the federal government. It would be too difficult, expensive, and time-consuming to replicate the existing infrastructure at another level. Furthermore, a fragmentation of these efforts would lead to suboptimal results.

When it comes to the catalytic role, however, perhaps state and local governments are better suited to the task. They are closer to their firms, understand their needs better, and see the results of any program more clearly and directly. In addition, the benefits of increased employment and revenues accruing at the state level, will also make it easier to develop a constituency in support of export assistance programs.

CONCLUSIONS

The export efforts of small- and medium-sized firms are generically no different from those of larger-sized firms. (21) All of them have to be able to develop a quality product, service or idea, to produce it at the right price, and to find a foreign buyer. Yet smaller firms have less resources and less flexibility in implementing export activities. They are generally ignored by profit-oriented service organizations, which prefer the larger firms as clients, (22) and are usually more in need of help since they are frequently less aware of the potential benefits of exporting, less confident about their ability to export, and less knowledgeable about how to do it and where to go for help. In addition, small- and medium-sized firms often cannot afford to pay as much for the assistance needed as can larger firms due to their resource limitations. (23) To become more active participants in international trade, these firms need to be provided with the knowledge and tools to conduct business internationally, and with an environment which allows them to trade. Export assistance programs from the public sector should only ensure that there will be a playing field, that the playing field is level, and that there are referees who enforce the rules. Private sector support services should then be encouraged to provide the support necessary for the individual players. The players, the ball, and some courage, however, need to be provided by our firms.

Table 1

Problems Encountered in
Finding a Level Playing Field

- Exchange Rates
- Competition
    - Subsidies
    - State Enterprises
    - Preferential Treatment
- Tax Policies
- Anti-Trust Statutes

Table 2

Export Transaction Problems

1. Sales Efforts
2. Pricing
3. Communication
4. Distribution
5. Product Adaptation
6. Getting Paid
7. Obtaining Market Information
8. Documentation
9. Providing Technical Advice
10. Providing Parts
11. Financing
12. Providing Repair Service

Source: Survey data of the National Center for Export-Import Studies at Georgetown University

Table 3

Classification of Firms

by Stages of Export Activity

Stage[a]	Past Export Volume (% sales)	Present Export Volume (% sales)	Future Export Volume (% sales)	Export Volume ($)	Length of Time Exporting	Personnel Committed to Exporting	Type of Countries Exporting to	No. of Export Customers	No. of Export Transactions
Unwilling	0	0	0	0	0	0	not applicable	0	0
Uninterested	<5	<5	<5						
Interested	<5	<5	>5						
Experimenting		>5	>5						
Experienced, small scale	>5	>5	>5	<100 000	>2 yr		Europe Far East South America Africa	10 or more	20 or more
Experienced, larger scale	>5	>5	>5	>100 000	>2 yr	≥1	Europe Far East South America Africa	10 or more	20 or more

[a] *Note* In applying this categorization to firms, assignments to classes were made on the basis of meeting all criteria. (That is, if a firm qualified for a particular stage in all criteria except one, it was classified as belonging in the next lower stage.)

Source: M.R. Czinkota and W.J. Johnston, "Segmenting U.S. Firms for Export Development," Journal of Business Research, Vol. 9, 1981, p. 356.

APPENDIX

COMPANY PROFILES AND EXPORT ASSISTANCE REQUIREMENTS BY INTERNATIONAL STAGES

Stage 1: The Completely Uninterested Firm

Profile

Most firms have an annual sales volume of less than $5 million and less than 100 employees. The main decision maker is the president. The firm does not export and does not plan to do so in the future. Management is not exploring the possibility of exporting nor will unsolicited export orders be filled. Management tends to believe that exports will not contribute to the firm's profits or growth.

Assistance Requirements

Raise awareness level of exporting.

Implementation Strategies

Increase communication that expounds the value of exporting on an unsolicited basis. Communicate the tangible benefits of exporting to such firms through trade associations and miniconferences. Use successful small exporters from a peer or reference group as role models, asking them to provide testimonials and case studies to firms not interested in exporting. Increase information dissemination showing the size and profitability of foreign markets. Increase international education in schools to foster awareness of the international marketplace. Publish regularly export activity figures by industry, export profitability statistics, and data about the impact of specific export activities on the balance of trade.

Stage 2: The Partially Interested Firm

Profile

Most firms have an annual sales volume below $5 million and less than 100 employees. The current average annual export volume is below $200,000, which is sold to less than ten customers. One quarter of the firms have actively sought their first export order. Almost half of the firms started exporting to Canada, to which they currently ship half of their exports. The president of the firm has the most input in the export decision; the marketing manager is a close second. Management knows that the firm has exportable products and tries to fill export orders. Management tends to believe that exporting may be a desirable activity and undertakes some exploration of export possibilities. Management is uncertain whether or not the firm will export more in the future and whether exports will contribute to the firm's growth and profits. The main reasons that motivate exporting are a unique product and profit advantage.

Areas that the firm tends to see as being somewhat of a problem in the export effort are financing, information on business practices, communications, providing technical advice, and sales effort. Firms believe that the Department of Commerce can be of substantial help to their export effort by assisting with obtaining financial information, financing, handling documentation, communications, and funds transfer.

Assistance Requirements

Raise awareness levels of export benefits; assist with information about the mechanics of exporting.

Implementation Strategies

Use case studies to demonstrate the benefits that can be derived from exporting. Increase communications to make firms more aware of existing services. Provide these services in a more accurate and timely fashion. Respond to export financing requests from such firms through more active small-volume export financing by Eximbank or by establishing a nonprofit facility that provides occasional exporters with small-sized credits (below $100,000) in a rapid fashion. An alternative could be a government guarantee of small export loans to banks similar to current student loan programs. Train Department of Commerce field officers to handle routine documentation problems and to have a general knowledge about the mechanics of the international transfer of funds. Hire more multilingual field officers so that they can assist with communication problems. Institute a centralized task force within the Department of Commerce which can provide rapid answers to field officers with nonroutine problems. Encourage universities to include commercial aspects in their foreign language courses. Create language banks at universities that, for a small fee, aid firms in translating foreign documents.

Stage 3: The Exploring Firm

Profile

Most firms have an annual sales volume below $10 million and less than 100 employees. These firms export about $500,000 worth of merchandise to less than 20 customers. More than one-third of the firms have actively sought the first export order, which mainly originated from Canada. Currently, about one-third of their exports go to Canada.

In management, the president is the major export decision maker. The desirability of exporting is well-known, as is the fact that the firm has exportable products. The firm is planning on exporting and is actively exploring export possibilities. The potential contribution of exporting to the firm's growth and profits is acknowledged, but past export profits have not met expectations. Having a unique product and obtaining a profits advantage are principal motivating factors for exporting. Important problems are encountered in the areas of communication, sales efforts, marketing information gathering, information on business practices, and obtaining financial information.

Assistance by the Department of Commerce is seen as valuable in the areas of obtaining financial information, information on business practices, marketing information gathering, handling documentation, and communication.

Assistance Requirements

Make exporting more profitable. Provide general information and practical assistance.

Implementation Strategies

An increase in deductions for export losses may help increase the profitability of exploring firms. The possibility of entering into risk- and profit-sharing agreements for a specified amount of initial exports with a governmental export intermediary should also be considered. Publication of books and brochures containing current general market data and a wide distribution of these publications would help satisfy the general information needs. Department of Commerce field officers should be trained in handling documentation problems of these firms. The use of multilingual officers and cooperation with universities as mentioned for Stage 2 would also help.

Stage 4: The Experimental Exporter

Profile

Most firms have an annual sales volume of less than $5 million and have less than 100 employees. Average exports are about $750,000 and are shipped to about ten customers. One-third of the firms actively sought their first export order, which came mostly from Canada. Currently, one-third of the exports go to Canada.

The president is the major decision maker. Exporting is seen favorably but little active exploration of export possibilities takes place. Principal motivating factors for exporting are a unique product, technological advantage, and profit advantage.

Important exporting problems are seen in the areas of sales efforts, obtaining financial information, physical product adaptation, marketing information gathering, and information on business practices.

Assistance by the Department of Commerce is seen as somewhat helpful in the areas of marketing information gathering, information on business practices, handling documentation, obtaining financial information, and communication.

Assistance Requirements

Encourage the active exploration of exporting. Provide general assistance and help with product adaptation.

Implementation Strategies

Provide foreign purchasing requests for products manufactured by these firms to management. Increase participation of these firms in foreign exhibitions. Search for contact for these firms and carry out initial contact for them. By functioning as an intermediary placing export orders with firms, an institution could clearly demonstrate the benefits of exporting without forcing firms to partake in the initial risk. Not only could such a step contribute to ~~the~~ fulfillment of affirmative action goals, but a measure of government effectiveness would also be introduced. Apart from the general assistance, increased information on foreign product standards should be communicated to these firms. Tax legislation that would permit increased deductions for costs incurred in product adaptations would help reduce the severity of this problem.

Stage 5: The Experienced Small Exporter

Profile

Average annual sales volume is below $10 million. Most firms employ less than 100 people. The export volume is slightly below $1.5 million and is shipped to an average of 40 customers. Four out of ten firms actively sought their first export order. One-third of the firms started their exporting to Canada, to which they currently ship one-fourth of their exports.

The president is the major decision maker with strong input from the vice-president for marketing. Exporting is seen in a very favorable light. Only the past profitability of export activities is called into question. Profit advantage, a unique product, managerial urge, and a technological advantage are the main factors motivating exporting. Problems encountered in exporting are important in the areas of communication, sales effort, marketing information gathering, obtaining financial information, and handling documentation. Assistance by the Department of Commerce is seen as somewhat helpful in the areas of gathering information on business practices, marketing information gathering, obtaining financial information, communication, and financing.

Assistance Requirements

Make exporting more profitable, provide general assistance, and help with financing.

Implementation Strategies

Financial assistance is now needed in greater size and for longer time periods than for firms in lower stages. Rapid responses to financing requests are not that important here. An increase in the cooperation with Eximbank will help satisfy this need. Training seminars on export financing would be of value to firms in this stage. Requests for financial information need to be responded to rapidly and accurately. Improvements in the training of commercial officers stationed abroad will help achieve that goal. By introducing a specific lead time of one week and assuming limited liability for incorrect information, such service would be more highly regarded, used more, and would strongly help firms in this international stage with their exporting efforts.

Stage 6: The Experienced Large Exporter

Profile

Most firms have an average annual sales volume below $50 million and employ between 100 and 250 persons. Average annual export volume is about $6 million, shipped to about 140 customers. About one-half of the firms actively sought their first export order. One-fifth of the firms began their export activities with Canada, to which they now ship one-eigth of their exports.

The president, together with the marketing manager, are the main export decision makers in the firm. Exporting is seen in a very favorable light with the firm planning to be continuously active in the future. Main motivating factors for exporting are profit advantage, technological advantage, competitive pressures, DISC legislation, a unique product, and managerial urge. Important problems are encountered in the areas of communication, sales effort, marketing information gathering, providing repair service, and information on business practices. Assistance by the Department of Commerce is seen as possibly helpful in the areas of marketing information gathering, information on business practices, obtaining financial information, financing, and funds transfer.

Assistance Requirements

Facilitate customer service and provide general assistance.

Implementation Strategies

To facilitate customer service abroad, companies should be encouraged to train foreign personnel enabling them to provide such services abroad. Such training costs, jointly with the indirect cost of customer service, such as the translation of repair manuals, should receive preferential tax treatment through multiple deductions in order to allow firms export expansion without strong hindrance by customer service cost consideration. A reassessment of the current taxation of U.S. nationals living abroad would also be helpful. The further granting of tax incentives to such firms should be reconsidered since they are currently satisfied with the profitability of the exporting efforts and sufficiently committed to the continuation of their international activities even without tax benefits.

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THE CAPITAL GAP
FACING
SMALL BUSINESS IN AMERICA

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THE CAPITAL GAP FACING SMALL BUSINESS IN AMERICA

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THE CAPITAL GAP FACING SMALL BUSINESS IN AMERICA

A. THE VITAL ROLE OF SMALL BUSINESS IN AMERICA

The increasingly important role which small business plays in creating jobs throughout America as been well documented. In order to continue to grow and expand, America's largest businesses are becoming more multi-national and world oriented. To remain price competitive in the highly integrated and competitive world economy, the giants of American business are forced to seek out the least expensive elements of production (i.e. raw materials and direct labor). Because many of America's inexpensively available natural resources have been exhausted and because we enjoy a high standard of living (i.e. because our cost of labor is high relative to other nations), America can no longer mass produce goods more cheaply than other nations in spite of our production technologies. To gain maximum competitive advantage, U.S. multi-national firms use their capital resources to construct new technologically advanced plants overseas, nearer the cheaper sources of raw materials and direct labor. As the newer plants come on line, older U.S. plants which become (or seem to become) less profitable or unprofitable because they employ higher priced labor inputs are closed. The net effect of this process in the world economy is to export U.S. jobs to foreign lands. While U.S. multi-national firms continue to grow in sales and profits, the number of American workers they employ diminishes.

As this process of investing U.S. capital into overseas plants continues and accelerates, the burden of creating jobs in America falls more heavily on the small business community. Small businesses have neither the management structure nor the capital resources to roam the continents in search of cheap labor. Instead, they thrive on the close management of their small operations and limited capital resources. In order to closely manage their operations, small business owners invest their limited resources into plants which are located in America and operated by Americans. As a result, small businesses create the bulk of new jobs in the nation.

Small businesses could not grow and prosper in the face of stiff foreign competition if they did not offer products and services at prices customers were willing to pay. They can and do survive becasue they fill important and growing market segments which cheap labor nations are not able to penetrate. Small businesses thrive on their ability to customize products and services, to perform short or long producton runs, to carry inventory for customers employing "just-in-time" inventory systems, to ship short and odd lot orders on a moment's notice, to provide quick turnaround time, and to provide close personal contact with customers whose needs and demands require a high degree of flexibility. Within the world economy, small businesses are like a fleet of small motor launches in a harbor filled with super tankers. While they cannot deliver vast quantities of product, they can turn on a dime and maneuver quickly. It is this flexibility and closeness to the market which enables them to thrive among the giants.

For the foreseeable future, this process of big business job exportation and small business job creation will continue. As long as foreign, multi-national firms based in Asia, Europe and elsewhere are equipped with the latest technologies and are willing to seek out the cheaper labor alternatives, U.S. multi-national firms will be forced to do the same. If the U.S. hopes to create sufficient jobs to employ the future adults of our nation, we must develop a national policy which fosters the growth of small businesses in America.

B. THE PLIGHT OF GROWING SMALL BUSINESSES

In spite of the important role small business plays in creating jobs in America, small businesses have always been thrwarted in their ability to reach their full growth potential. Financing, the lubricant or fertilizer necessary for proper growth, has never been available to small businesses in the amounts or under the terms necessary to foster and facilitate growth. As a result, America has been robbed of the creation of thousands of new private sector jobs annually.

To meet their full growth potential, small businesses, like all businesses, need two types of financing. First, they need access to longer-term, fixed rate, reasonably priced financing for capital expenditures and explansion (i.e. for plant and equipment). Secondly, as growth occurs, they need supplemental debt and equity to increase their working capital base (i.e. they need to increase receivables and inventory) to support a larger sales volume.

Capital expenditures provide a small business with the wherewithal to increase production and employment (i.e. to create new jobs). Very basic financial management principles suggest that to properly manage a company's assets and liabilities, the balance sheet should be structured in such a way that the term or maturity of the financing (i.e. the liabilities) underlying the capital expansion should be matched to the life of the capital assets being financed. This basic tenent of finance is known as "matching sources and uses of funds." Proper matching of sources and uses of funds will enable business to make debt service payments from the revenue stream generated by the asset over the asset's economic life. If the revenue stream does not exceed the debt service by some margin, the investment makes little economic sense and probably should not be undertaken. In the modern business world, large national and multi-national firms, who have a wide variety and a multitude of financing options available to them, pay little heed to the matching of sources and uses precept, sometimes with dire consequences. To small businesses, with few financing options and alternatives, however, this precept remains a critical parameter of success and survivial.

A major plant expansion by a small business might involve purchasing capital assets including land, building and capital equipment with long economic lives in excess of 20 years or more. To properly match the financing underlying the capital assets, the small business needs to have access to longer-term financing with maturities exceeding 20 years. The capital markets in America are illequipped to provide such financing to the small business community.

Capital expansion financing, however, needs to be more than long-term. It also needs to be available on a fixed interest rate basis. Floating or variable interest rates only add mountains of risk and uncertainty to the already risky and uncertain proposition of operating a small business. When it comes to mortgage financing, a small business often looks more like an individual homeowner than a corporate giant. For an individual homeowner, the amount of mortgage financing he/she obtains is large relative to the annual income of the individual. As a rule of thumb, a homeowner can afford mortgage payments which consume up to 25-30% of one's income. In the case of a small business, the debt service on capital financing, while not as large as the debt service an individual homeowner faces, may consume up to 10% of a company's sales. It is not unreasonable for a small business to earn a profit before debt service of about 15% of sales. If debt service consumes 10% of sales, the entrepreneur or small business retains a profit margin of about 5% of sales after debt service. If mortgage rates on a floating rate mortgage rise by (say) 3-4%, the entrepreneur may find that the increase in debt service virtually wipes out the company's profits. From the entrepreneur's point of view, he/she ends up "working for the bank". Large businesses insulate themselves from interest rate fluctuations by accommodating their capital needs through the long-term bond markets which offer fixed interest rates. Small businesses have no such ready access to the long-term bonds markets and are thus saddled with floating interest rate risks on their capital expenditures. The uncertainty caused by floating or variable interest rates often makes borrowers less aggressive in their expansions than they otherwise might be and lenders more cautious. Lender caution may be expressed by requiring a larger down payment or a higher debt coverage ratio threshold than might otherwise be required on a fixed interest rate loan. Either way, the result of the added risk and uncertainty is less availability of financing, smaller or curtailed expansions, and fewer jobs created by small business.

In addition to being fixed, interest rates need to be reasonable. Large, multi-national firms usually can borrow funds on a long-term, fixed rate basis through the national bond markets at interest rates which are only slighly above the U.S. Treasury's borrowing rates. Small businesses, on the other hand, often face rates of interest which are 3-4% or more above U.S. Treasury bond rates. In today's market, small businesses might be paying as much as a 50% higher interest cost than the large multi-national firms. As a result, a small business has less debt capacity per dollar of debt than the larger firm. For example, if a small business had $600,000 of funds available for annual debt service, it could afford a plant expansion of $6.1 million if it were able to borrow the funds at 7½% (near U.S. Treasury bond rates) over a 20 year term. At 10½% (a more likely long-term interest rate for a small business - if the term were available at all) the same company could afford a plant expansion of only $4.9 million, a 20% reduction in project size. Assuming a small business can create one new job for every $25,000 of new plant investment, the cost of financing alone would have prevented this single company from creating 48 additional jobs. When a 20% reduction in each expansion is multiplied by the number of small business expansions occuring annually, it is apparent that America loses the creation of hundreds of thousands of jobs annually as a result of the price of the financing. Unfortunately, the problem is exacerbated further because most small businesses cannot find 20 year term financing at any cost. The primary providers of financing for small businesses, commercial banks, cannot make 20 year financing widely available.

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Thus, long-term, fixed-rate, and reasonable price are the sine qua non for proper plant expansions. Large multi-national firms have access to such financing. They, however, create jobs overseas. Small businesses, the companies creating jobs in America, have no such ready access to proper financing. Because America's job creators are placed in a competitive disadvantage with the foreign job creators, America robs itself of thousands of jobs annually.

C. WHY THE LONG-TERM CAPITAL GAP EXISTS

Small businesses are unable to obtain proper financing for their plant expansions because they have no ready access to the long-term capital markets in America. Access to the long-term credit markets can be gained through either of two routes: a public offering or a private placement. Three obstacles lie in the path of a small business desiring to obtain credit through a public offering:

1) The cost of entry into the market often is exhorbitant
2) The company's credit worthiness is unrated
3) The project is too small to sustain a market

In order to issue debt intended to be held by the public at large, the debt issuer must file an SEC registration which often costs in excess of $150,000. To prepare a prospectus for filing with the SEC, a major accounting firm must audit and certify the company's financial statements, a myriad of legal documents and opinions must be prepared, obtained, and reviewed, and an investment banker must find buyers interested in investing in the borrowing company. Because the typical small business expansion costs less than $1.0 million, a $150,000 or higher cost of issuance normally makes the public issue economically unsound. Eventhough amendments to Regulation D of the Securities Act of 1933 simplifies the public issuance process and makes it less costly to issue securities, this hurdle combined with the other two hurdles make a "going public" the exceptional rather than the normal way of obtaining financing.

The second impediment facing a public issue by a small company is the creditworthiness of the borrower. To be publicly traded, a company usually needs to be rated by Standard & Poor's or by Moody Investors. Most small businesses have never been rated at all. If they attempt to secure a rating, they will find that, almost by definition, they will be rated below "investment grade" quality because they lack size and muscle in the marketplace. In the eyes of rating houses, in order for an investor to be secure in investing in a stock or bond, that is, in order for an issue to be rated "investment grade" quality, the company must be large enough to attract broad market interest in the security even in prolonged downturns (i.e. there must be many shares and lots of willing investors to ensure liquidity in the stock or bond), while the company's operations must be sufficiently large and diversified to permit the company to weather severe recessions. In other words, the company must be large and very healthy in order to be rated "investment grade" quality. Without an investment grade rating, the number of market investors willing and able to invest in the company is substantially reduced. For example, almost all mutual and pension fund investments by law must meet investment grade standards. While unrated issues do trade in the market, the market labels such issues "junk bonds", a term which aptly describes the market's attitude to such issues. Junk bonds do have the advantage that they provide a borrower with long-term maturities and fixed rates of interest. The cost of borrowing, however, is high as a result of a combination of hefty fees charged on the front-end, the need to establish a large debt service reserve to replace the unobtainable rating, and a higher coupon yield on the bond. In addition, to entice an investment banker to issue a junk bond, the size of the issue must be much larger than the typical small business expansion of $1.0 million or less. To keep the hefty front-end fees reasonable, investment bankers attempt to spread them over a larger issue, normally in excess of $10.0 million. If a $1.0 million junk bond were issued, the front-end fees could easily exceed $100,000, 10% or more of the total issue.

The final obstacle to a public issue by a small business is the size of the issue. One of the primary advantages to investors in publicly traded securities is liquidity of investment. If investors need to raise cash, they can readily sell their publicly traded stocks and bonds to third parties in a matter of seconds. In order for liquidity to exist in the market, there must a large number of third parties who know about the company and who are interested in owning it. To gain the necessary market recognition and acceptance the issue must be broadly traded. In other words, there must be large number of shares of stock or debentures outstanding. A $1.0 million or less issue simply is too small to create the necessary market recognition and acceptance. Without a broad market, liquidity disappears and with that one of the primary reasons for investing in publicly traded issues is gone.

These three hurdles effectively slam the door on public issues by small companies. The cost of issuing $1.0 million or less of publicly traded securities is too high to make it a viable vehicle for most expansions. The lack of an S&P or Moody's rating eleminates an enormous number of potential buyers. The inability for a small issue to create a broad and liquid market destroys a major advantage of purchasing a publicly traded security. What is left is a small number of companies who issue restricted securities under Regulation D to a few number of investors who are patient and willing to forego liquidity in the investment.

The second avenue into the long-term capital markets is through a private placement. A private placement avoids some of the problems inherent in a public issue. Without an SEC registration, the cost of entry is substantially reduced through a private placement eventhough rigorous financial audits must be performed and a battery of attorneys must sign-off on the project. The investor in a private placement, normally a pension fund or a large insurance company, or, less frequently, another business is a fairly sophisticated market investor who understands that the private placement has no liquidity (and prices the placement accordingly). But three substantial obstacles remain which block small businesses' access to the private placement market. First is the company's lack of an investment grade rating. Pension funds exist to provide an income stream to pensioners during their retirement years. To safeguard the national interests of retired persons, pension funds by law must restruct themselves to investments with "investment grade" ratings, a rating a small business is unable to obtain. Large insurance companies which provide both pension and death benefits, face some of the same impediments to investment in unrated companies through regulation by the State Insurance Commissioner.

The second hurdle facing a small business attempting a private placement is the size of the issue. Pension funds and insurance companies are enormous financial institutions whose typical transactions are in multi-million dollar increments. They simply are not interested in small investments of less than $1.0 million. Unless several issues are bundled together, a small business private placement will never occur. Bundling and pooling are unwieldy processes in the eyes of pension funds and insurance companies which prefer simple "buy and sell" transactions.

The final issue facing private placements is servicing the loan or investment. Large financial institutions dealing in multi-million dollar increments, located many miles from the borrower simply do not have the ability to service a loan of less than $1.0 million. Without local presence, the relationship is not properly monitored or serviced. As a result, pension funds and insurance companies avoid building a portfolio of small geographically diverse loans.

Because of these impediments to both public issues and private placements, small business are forced to satisfy their credit needs elsewhere. They end up borrowing from their local commercial bank or, less frequently, from the local S&L. Local commercial banks have the local presence necessary to monitor and service smaller relationships well. Commercial bank loan officers understand a small business and the entrepreneur better than a large institutional investment advisor. And banks are well equipped to handle smaller transactions. Local commercial banks, however, are short term lenders, a factor which cripples their ability to fill the long term capital gap.

D. COMMERCIAL BANKS ARE SHORT-TERM AND FLOATING RATE LENDERS

Small businesses are unable to obtain proper financing for their plant expansions because they have no ready access to the long-term credit markets in America. Instead, the primary suppliers of credit to small businesses are local commercial banks. Commercial banks fill many roles in the U.S. economy, but none is more critical than providing stability and liquidity to the U.S. monetary system. To protect the stability and needs of the monetary system, the Federal Reserve, the Comptroller of the Currency and a host of state regulatory authorities highly regulate the commercial banking industry. One form of liquidity regulation is the requirement that banks rigorously match their own sources and uses of funds. In order to be liquid, a commercial bank must structure its uses of funds (loans to customers) so that they mature and are collected and available to a depository customer (a source of funds) when that customer demands payment. A commercial bank's sources of funds are predominantly short-term deposits including demand deposits (i.e. checking accounts), time deposits (i.e. savings accounts), and short-term money market investment accounts and certificates of deposit. The average maturity of these sources of funds is far less than 3-5 years. A commercial bank's uses of funds primarily consist of loans to customers and purchases of U.S. government obligations. To properly match their uses of funds with their sources of funds, commercial banks are required to restrict their loans to customers to relatively short maturities, because the majority of the sources of funds may be withdrawn over the very near-term. A loan to a customer is a legally binding contract which permits the borrower to use funds for a specific period of time. The loan maturity may not be accelerated unless the borrower defaults on a loan covenant or fails to make a payment. Because the bank cannot call the loan for another reason, such as the bank needing the cash to honor a withdrawal request, the bank will keep its loan portfolio liquid by keeping maturities very short-term. The most common bank loans to businesses are 90-day notes. Typically less than 10% of a bank's business loan portfolio has a maturity in excess of 7 years. In other words, in order to safeguard the liquidity requirements of our monetary system, commercial banks are not permitted to provide a small business with long-term financing would properly match to the life of the assets acquired during a plant expansion.

The short-term nature of the bank's deposits also prevents the bank from making fixed rate loans to customers. Because CD's and other interest-bearing depository accounts at commercial banks mature over the very short-term (generally in less than a year), the bank's cost of funds will rise and fall quickly in accordance with general money market conditions. If a bank would fail to raise its rates on its CD's and other interest bearing accounts as general interest rates rise, it would lose deposits as the short-term deposits mature. In order to protect the stability of the banking system, commercial banks must raise the interest rates on their longer-term loans to customers if their cost of funds (interest on deposits from customers) rises. If they fail to pass along the increase in interest costs, the commercial banks could suffer large operating losses which could threaten the overall stability of the monetary system. In the early 1980's, the thrift institutions suffered large losses because their residential mortgage loan portfolios consisted of long-term, fixed interest rate loans while their deposits from customers were short-term money market and pass book accounts subject to rate volatility. As interest rates rapidly rose in the late 1970's, S&Ls were forced to raise interest rates on deposits while interest rates on their loan portfolio were fixed causing a severe price-cost squeeze. To the degree the thrift institutions resisted rate rises on deposit accounts to prevent a negative spread between loans and deposits, they suffered rapid run-off of deposits. The thrift industry has yet to fully recover from its crisis.

To prevent such a crisis in the commercial banking industry, commercial banks routinely make loans on a variable or floating rate basis. When some index, normally "prime" rate, rises the rate of interest on virtually every business loan in the bank's portfolio rises by some amount. In this way, the commercial bank maintains a positive spread between its loans and cost of funds and the stability of the commercial banking industry is better preserved.

Commercial banks use their funds for more than just making loans to customers. They also purchase U.S. government obligations, that is, they also make loans to the U.S. Treasury. When we look at a bank's portfolio of loans to the U.S. government, however, we see an entirely different set of maturities than we observed when looking at loans to customers. Banks will purchase U.S. government securities with a very wide spectrum of maturities, from short-term U.S. Treasury Bills which mature in less than one year to long-term U.S. Treasury bonds and other agency debt maturing in 30 or more years. In spite of the distant maturity dates, commercial banks typically are able to hold securities bearing both long and short maturities because U.S. government debt is highly liquid regardless of its maturity. Should the bank need to raise cash to honor withdrawal demands by customers, the bank can sell these long-term U.S. government obligations into a very large, well established, and liquid secondary market for U.S. Treasury obligations. Because the secondary market is always available to purchase the securities from the bank, the bank and its regulators view these assets as assets which match the life of their deposits (very short term). In other words, the existence of the secondary market permits commercial banks to maintain a high level of liquidity while providing the U.S. government with access to long-term, fixed interest rate financing. In sum, both U.S. multi-national firms and the U.S. Treasury have access to long-term, fixed rate, reasonably priced debt. Because small business, America's chief job generator, has no such access. To the long term capital markets, it cannot achieve its full growth potential and the nation is robbed of thousands of new jobs annually.

E. A PARALLEL EXAMPLE IN HOUSING

Commercial banks are the appropriate sources of capital for small businesses because of their of their ability to service and monitor smaller borrowers, their proximity to their customer, and their ability to handle transactions of less than $1.0 million. Regulations which are intended to protect the national interest of a liquid and stable monetary system, however, prevent commercial banks from making long-term fixed interest rate financing available to small businesses. Commercial banks, on the other hand, do provide long-term fixed interest rate credit to the U.S. Treasury because of the existence of a large, well established and liquid secondary market willing to buy the U.S. Treasury Bonds from the bank should it need cash. The existence of the secondary market enables the bank to make loans which are long-term yet highly liquid. The same situation exists in the market for residential mortgages. Commercial banks are able to make long-term fixed interest rate home mortgages because in the national interest Congress has created a large, formal, well established secondary market to purchase home mortgage loans from local lenders should they decide to sell them, which they normally do. Through the home mortgage secondary market, local lenders can make home mortgage loans which are long-term yet highly liquid. In the process, a small individual home owner gains access to the long-term credit markets.

The secondary market process is quite simple. A local lender originates small individual loans which it commits to sell to an intermediary. The intermediary pools these mortgages into a sizeable security known as a mortgage backed security or a collaterized mortgage obligation (CMO for short) because the underlying home mortgages become collateral for the larger security instrument. The larger security is then sold to large long-term investors such as pension funds, mutual funds, portfolio managers of investment banking houses, insurance companies, bank trust departments, wealthy individuals etc. In other words, through the secondary market, the obstacles which impede a small business access to the long-term credit markets are surmounted. The home mortgage secondary market primarily consists of three major intermediaries: the Federal National Mortgage Association (FNMA or "Fannie Mae"), the Government National Mortgage Association (GNMA or "Ginnie Mae"), and the Federal Home Loan Mortgage Corporation (FHLMC or "Freddie Mac").

The Federal National Mortgage Association (FNMA) was established in 1938 as a subsidiary of the Reconstitution Finance Corporation pursuant to Title III of the National Housing Act. Its primary function, until 1972, was to purchase FHA-insured mortgages from private lenders, thereby assisting the secondary mortgage market to replenish the supply of mortgage capital at the originating lender's level. Mortgages purchased by FNMA theoretically are held and resold when mortgage money is more plentiful. In essence, FNMA acts like a "Specialist" on the New York Stock Exchange, dealing in a simple commodity, home mortgages. In 1968, FNMA was split-off from the U.S. government and became a government sponsored, but privately owned corporation capitalized, in part, by the U.S. government. Between 1972 and 1974, FNMA's authority was expanded to include, in addition to its long standing role of purchasing FHA-insured mortgages, purchasing conventional home mortgage loans and condominium and Planned Unit Development (PUD) projects. Today, FNMA which is the heart of the secondary market system in home mortgages funds its operations ~~in a~~ variety of ways including:

1) Sale of common stock.

FNMA sells its shares of common stock through the New York Stock Exchange to captive stockholders which consist of lenders who sell their mortgages to FNMA. These captive stockholders must commit to purchase and hold a certain amount of stock based upon the volume of mortgages sold to FNMA, not to exceed 2% of the unpaid principal balance of the mortgages purchased by FNMA from the seller.

2) Sale of Debt & CMOs

FNMA also issues notes, debentures, and mortgage backed bonds to finance its purchases of mortgages. Because most of the mortgages purchased are either FHA-insured on GNMA-guaranteed, FNMA's debts carry a Corporate AAA rating.

3) Sale of Purchased Mortgages

FNMA can sell the mortgages it purchases when money market conditions are appropriate. In reality, FNMA seldom sells more than a nominal amount of the mortgages it purchases.

4) Fee Income

FNMA also charges a variety of fees for its commitment to purchase mortgages from local lenders.

GNMA was created in 1968 as FNMA was being converted into a private corporation. Housed in the Department of Housing and Urban Development, GNMA was created to support the "special assistance" functions which FNMA had previously handled prior to becoming a private corporation. In addition, GNMA was given the responsibility for establishing a mortgage backed security program. Under its special assistance function, GNMA purchases mortgages which would otherwise not be readily salable except at deep discounts because of the high risk of the project or the low coupon rate on the mortgage. By making a market for these otherwise undesirable mortgage loans, GNMA has the effect of stimulating private development of hard to finance housing because lenders can be assured of receiving 100% of the face value of the mortgage without undue discount due to the mortgage's unattractive features (high risk or low rate). GNMA borrows from the U.S. Treasury to finance these purchases and simultaneously resells them to FNMA or other purchasers through its Tandem Plan. GNMA absorbs any loss to due to the discount in the sale to FNMA or other purchaser.

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GNMA also has the authority to guarantee the timely payment of principal and interest of certain securities backed by FHA, VA, or FmHA-insured mortgages. Under the authority, an FNMA/GNMA approved lender can issue a long-term debenture backed or secured by a pool of mortgages which are U.S. government guaranteed. GNMA will guarantee the buyers of the long-term debenture the timely payment of principal and interest. Because the GNMA guarantee has the full faith and credit of the federal government standing behind it, GNMA guaranteed securities trade near U.S. Treasury bonds (better than FNMA rates which are traded near corporate AAA bonds). Under the mortgage backed security program, the eligible issuer, an FHA-approved mortgagee, pools government guaranteed mortgages which become collateral for the security or debenture. The issuer services the mortgage. The pool must be homogenous with respect to interest rate and type of dwelling. While maturities need not be identical, similar maturities are preferred. Mortgages constituting the pool must have been insured within 12 months from the date of GNMA's guarantee commitment. The pools are sold to large investors and small. Buyers include pension funds, REITs, insurance companies, trusts, and wealthy individuals. Should the GNMA guarantee be called, GNMA may borrow from U.S. Treasury until it has the time to foreclose and collect on the instrument through the appropriate federal agency.

The Federal Home Loan Mortgage Corporation (FHLMC or "Freddie Mac") was established in 1970 by the enactment of Title III of the Emergency Home Finance Act of 1970. Freddie Mac, which is owned by the 12 member banks constituting the Federal Home Loan Bank System, the regulatory authority for the S&Ls and Savings Banks, in effect created a FNMA for thrift institutions. Under its authority, Freddie Mac purchases federally guaranteed and conventional home mortgages from S&Ls to replenish the liquidity of the local S&Ls who can then originate additional home mortgage loans. It is capitalized and finances its operations similarily to FNMA:

1) Sale of common stock

The initial funding of $100.0 million was obtained through the sale of stock to the twelve Federal Home Loan Banks.

2) Sale of CMOs and other debt

Freddie Mac also sells mortgage backed securities guaranteed by GNMA or by itself. Its CMOs are known as "Participation Certificates" (PC). In addition, Freddie Mac can also issue its own debt into the capital markets.

FNMA, GNMA, and Freddie Mac constitute the secondary market for home mortgages. Together, they provide individual homeowners with billions of dollars of access to the long-term capital markets annually. A similar secondary market for small business plant expansion loans would enable commercial banks to originate long-term fixed interest rate loans which could be pooled and sold into the long-term capital markets. Such a secondary market would serve two national interests: helping small businesses to create new jobs while safeguarding and enhancing the liquidity and stability of our monetary system. And a secondary market would enable small businesses access to the same financing terms and conditions already available to the U.S. Treasury, large multi-national corporations, and individual homeowners.

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F. THE REQUIREMENTS OF A SECONDARY MARKET

To establish an active and working secondary market for small business capital expansion loans, there must be four kinds of participants: businesses wishing to borrow, originators willing to lend, investors interested in buying the securities, and an intermediary willing to oblige the needs of the orginators and investors.

Potential small business borrowers will look for three features in the secondary market:

- Inexpensive cost of entry
- A simple and timely process by which loan applications are processed and approved and loans are closed and disbursed.
- Loans which are long-term, have fixed interest rates, and are reasonably priced.

Small business entrepreneurs are not patient people. Once they have decided on an expansion, they will be anxious to move ahead. They can be expected to select improperly structured but timely delivered financing rather than waiting an inordinately long period of time for the right kind of financing. The secondary market must therefore be able to process applications quickly. Self-approval by the originating lender could insure a timely processing system which meets the needs of a small business. Regulations and eligibility criteria need to be simple, straightforward and based on common sense. The borrower and the originator should have a fair idea in advance of whether or not the application will be approved. In the national interest of assisting small businesses to create jobs through properly structured financing, the secondary market should be structured to encourage rather than discourage the participants from using the market.

Commercial banks will be the most likely, but not exclusive, originators of small business loans. They will look for many of the same ingredients in a secondary market that the small business borrower looks for including the following:

- A simple, straightforward application process which delivers commitments in a timely fashion.
- A set of eligibility and use-of-proceeds regulations which are structured to simplify rather than complicate the process of delivering long-term financing to their customers.
- A firm commitment from the intermediary to purchase the loan upon the completion of construction.
- A routine, clean system of closing and disbursing loans.
- A fair servicing fee.
- Timely and periodic sale dates with immediate funds transfer.

Because the originators, commercial banks, cannot have substantial holdings of long-term loans in their portfolios, they need to be assured that they can sell all of their long-term loans in their entirety on a routine basis. Forward commitments at a firm price probably will be necessary.

Investors most likely will expect four features in the secondary market:

- Safety and security of investment capital
- Liquidity
- Market yield on invested capital
- Standardized and homogenized investment units

To provide the safety and security of investment capital, the secondary market probably will have to offer a full faith and credit instrument of the U.S. government. To provide the necessary liquidity, the intermediary or other participant should stand ready to repurchase the securities if and when necessary. A market rate of return on invested capital, if the security is backed by the full faith and credit of the U.S. government, will be near Treasury bond rates. Standardized units of investment can be created through participation certificates of $1,000, $10,000 or $25,000 units. Pools can be aggregated with common maturities of (say) 10 and 20 year maturities.

G. A SECONDARY MARKET FOR SMALL BUSINESS LOANS

In the national interest of creating jobs through small business expansions, a national secondary market for long-term small business loans is warranted. Precedent and a parallel structure already exist in the home mortgage industry. A secondary market for small business loans could borrow heavily from the ground already broken by FNMA and GNMA. The small business secondary market could be structured as either a private corporation like FNMA or as a governmental agency, like GNMA. Like FNMA, the small business loan secondary market could capitalize itself through both the federal government and the private sector. Like Freddie Mac, equity could be purchased by the Federal Reserve Banks (governmental participation) and, like FNMA, more equity could be raised from member banks (and non-bank lenders) who would be required to purchase and hold equity in accordance with the volume of loans sold to the intermediary. Similar to FNMA and Freddie Mac, the small business loan secondary market could be permitted to purchase both government guaranteed and conventional loans. Government guaranteed (SBA, EDA, FmHA B&I) loans could be purchased without additional credit scrutiny. Conventional loans would have to meet certain underwriting criteria. Credit tests would be performed and certified by the originating lender. Upon lender certification, sale to the secondary market would be automatic. Loans sold to the secondary market would be sold in their entirety without general recourse, in order to permit the originating local lender to remain highly liquid, but some form of risk sharing could be built into the approval process (e.g. the first $100,000 of loan could be sold with a repurchase agreement triggered upon default). Orginating lenders whose credit standards failed to be maintained at a high level would be denied access to the secondary market except through government guaranteed loan programs. To finance the acquisition of the loans purchased from originators, the secondary market intermediary could issue collaterized mortgage obligations (CMOs) which, like GNMA, would carry the full faith and credit guarantee of the U.S. government. The guarantee will enable the secondary market to achieve the following:

- Guarantee safety of investment to the investors
- Provide liquidity, broad market acceptance, and access to the nation's largest financial institutions, pension funds, insurance companies, and mutual funds.
- Provide small businesses with reasonably priced financing (near Treasury Bond rates).

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The pools underlying the CMOs could be homogenous in terms of rate of interest and maturity (such as 10 and 20 year CMOs) or alternatively could be structured as serial bonds. Like Freddie Mac's CMOs, the small business secondary market could sell its CMOs through "Participation Certificates" in denominations as low as $1,000 and as high as $100,000 to satisfy both the small individual and large institutional investors alike.

The small business loan secondary market would make long-term, fixed interest rate financing at near Treasury bond rates a reality for small businesses. It would enable local commercial banks to make long-term fixed rate loans without jeopardizing their liquidity which is necessary for a stable monetary system. In addition, it would permit large institutional investors to finance a segment of the market from which they are now excluded. And, finally, it would permit our government to facilitate the job creation process at home in America.

H. A WORD ABOUT SBA CERTIFIED DEVELOPMENT COMPANIES

SBA has two major loan programs under its legislative jurisdiction: the Section 7(a) Loan Guarantee Program established under the authority of the Small Business Act of 1952; and Section 502/503/504 Development Company Loan Programs established under the authority of the Small Business Investment Act of 1958. The Development Company loan program underscores the importance of the concepts presented in this paper. Under section 502/503/504 locally organized and controlled Certified Development Companies (CDCs) are licensed by the SBA to provide long-term, fixed interest rate subordinated mortgages to successful, growing small business expansions. In 1980, under Section 502, its funding level stood at $50.0 million annually. Use of the program expanded to a level of $400.0 million under Sections 503/504 in fiscal year 1986. Under the program, SBA finances 40% of the project cost of a plant expansion (including machinery and equipment) behind a 50% first mortgage made by a commercial bank. The 10% balance of the project cost is provided by the borrower's equity funds.

In total, SBA's 504 CDC Loan Program has financed $1.0 billion of small business expansions in fiscal 1986. The program has proven to be effective, popular, and prudent. While most domestic programs were being trimmed in the early 1980s, Congress expanded the CDC program. The lending authority has always been fully utilized and loan losses have been low. Best of all, the financing is creating one new job in America for much less than every $25,000 of fixed asset investment.

Under Section 504, the SBA guarantees 100% of a second mortgage debenture which is advanced to the small business by the local CDC. The CDC debentures are pooled by the SBA and sold to market investors through Merrill Lynch & Citicorp. In essence, the SBA is creating, on a limited scale, a form of the small business secondary market described herein. With the full faith and credit of the U.S. government behind the mortgage debentures, the obstacles hindering small business access to long-term credit are substantially removed. Because there is no rigorous SEC registration required for each small business debenture, the small business avoids the potentially prohibitive cost of issuance. Because the

SBA provides a full faith and credit guarantee, there is no need to seek out the unobtainable S&P or Moody's "investment grade" rating. And because the debentures are pooled, large institutional investors can participate in a meaningful way. In other words, the SBA 504 program provides small businesses for the the first time with access to our nation's long-term credit markets.

SBA 504 is an important first step in creating a small business loan secondary market. The problems with 504 are threefold. First, the $400.0 million is inadequate to do the job. Second, the program depends on the willingness of local commercial banks to make a moderately long-term (10 years or more) first mortgages. Prohibitive bank policies regarding long-term mortgages makes the CDCs' job difficult. Finally, there really is no secondary market. Section 504 paper is placed in the market, but there needs to be a formal secondary market intermediary, like FNMA, to make a market and insure liquidity.

Nationwide, there are about 500 Certified Development Companies licensed under Sections 503/504 to package subordinated mortgage financing for small business plant expansions. CDCs are highly professional, locally visible originators of financing. As licensed by the SBA, they are authorized to package, make, and service the second mortgages they originate. The have also been very effective advocates for small business at the local level. It is important that they remain integrally involved in the secondary market process, perhaps as the local clearinghouse for all secondary market financing in the community. Because of their skills at originating, packaging and servicing loans, they can provide continuity and momentum as the secondary market evolves. In essence, they can serve in a role parallel to that of the FHA-approved lender for housing loans.

L THE NEED FOR NON-DILUTING EQUITY

In addition to long-term financing for their plant expansions, growing small businesses need additional working capital. Commercial banks are much better prepared to help small businesses with their working capital needs than with their plant expansion needs. There are however, limits to what they can do.

Small businesses tend to be more highly leveraged than large, multi-national corporations. As was discussed earlier, small businesses are severely handicapped in their ability to enter either the public markets or private placement channels. Because of the high cost of issuance, the lack of an "investment grade" rating, and the inability of a small issue to support an active and liquid market, equity, like long-term debt, is beyond the grasp of most small businesses. Venture capitalists nominally do provide equity to small businesses but their scope of the market is so narrowly limited to high technology, computer, and bio-technology industries that the typical, strong, healthy, moderately-to-rapidly growing small business is too mundane for the venture capitalist. As a result, the equity base of a small business usually is limited to the initial owner's investment plus the company's retained earnings saved over the life of the business. The large Fortune 1000 business, on the other hand, can supplement its equity base and fortify its balance sheet by issuing new equity in the market when market conditions are attractive. This dichotomy between the availability of equity to a small business and a large company forces the small business to carry relatively more debt than a large company, that is, to be more highly leveraged than a large company.

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When any company grows (i.e. when sales rise), it first needs additional inventory to support its higher level of sales. By ordering additional inventory, its accounts payable rise. Accounts payable are a debt owed to trade suppliers. With more inventory, the company works its direct labor longer to create more finished goods. The additional input of labor causes accrued expenses, in the form of wages, payroll taxes, fringe benefits, etc., to rise. Accrued expenses are a debt owed to company employees. To pay accrued expenses, the company may borrow under its line of credit at its bank, creating a note payable, a debt to the local bank. In other words, as sales rise, debt begins to rise relative to equity. If the company earns a 15% profit margin on sales, it must sell about 6 units of inventory in order to create a profit sufficient finance one new unit of inventory with equity. In other words, as sales rise, debts owed to suppliers, employees and the banker may rise 5-6 times faster than equity. As a result, leverage in the company risess. At some point in time, the large company intercedes by entering the capital markets to obtain more equity to reduce the amount of debt relative to equity. The small business, however, has no such recourse to the equity markets. As a result, the small business tends forever to be playing catch-up. As trade debt rises, the company borrows from the bank and swaps an account payable or accrued expense for a note payable. The amount of debt relative to equity is not reduced. If growth continues, the small business finally reaches the point at which its suppliers and its bank stop advancing more credit. At this point in time, the company's ability to grow becomes limited by its leverage and its profit margins. Opportunities are missed and the company fails to achieve its full growth potential. When a natural slackening in the market for the company's product occurs as a result of a cooling-off of the economy or market satiation, the company finds itself at a lower level of sales and retained earnings than it otherwise would be.

This start-and-stop nature of growth in the economy is natural to all companies. When any business, large or small, grows rapidly, its need for cash outstrips its ability to generate cash from profits. At this point in time, debt begins to increase relative to equity. Large companies have the ability to supplement their equity base through external sources. Small businesses do not If market conditions are not suitable for selling new equity when the need arises, the large company can approach a consortium of lenders who will advance credit under a revolving line of credit (a "revolver" for short) under the assumption that the revolver will be repaid through an equity issue. In effect, the debt is treated as a bridge loan to equity by the lenders who deceive themselves into believing that the revolver is as good as equity. As a result, large businesses can continue further along the natural growth curve of the business cycle than can small businesses. The net effect is that small businesses never reach their full growth potential. When the downturn in the economy finally occurs, they have smaller sales and equity bases from which to start the next cycle.

To correct this imperfection in the market, small businesses need access to non-diluting equity which can be used to supplement the company's initial capitalization and retained earnings. The supplemental equity can be used by the business to adjust the amount of debt relative to equity. With a larger equity base, the small company will be able to leverage additional sources of debt. With access to more debt and equity, the small business will be able to ride further up natural growth cycle curve. When a slackening in the economy occurs, the company will find itself operating at a higher level of sales and with greater retained earnings.

The non-diluting equity a small business needs should have four primary features:

- first, it should be non-diluting. The typical small business has little desire in going public. There is no reason for the entrepreneur to give up voting shares or control of the board to a financial entitywhich has no interest in managing the company. In other words, the equity need not look like venture capital.
- second, it should not be expensive. Venture capitalists look for compounded rates of return in excess of 25% p.a. If non-diluting equity demanded a similar rate of return, it would eat up over 100% of the company's profits within a short period of time.
- third, the return paid to the investor should be in the form of tax-deductible interest expense, that is, the non-diluting equity should be structured as subordinated debt.
- fourth, it should be available for a term of 5-10 years to permit the owners sufficient time to repurchase the non-diluting equity in an orderly fashion. Incentives can be built in to induce the entrepreneur to repurchase the non-diluting equity early if so desired.

Four other features could be added to the non-diluting equity debentures to make them more attractive to investors. First, the interest earned by the investors could be made exempt from income taxes. Alternatively or additionally, the debenture could be established as an asset which could be amortized over (say) five years. In addition, the debenture could be structured as a zero coupon bond, the implied interest on which could be tax-deferred until collected at maturity or sale. Finally, warrants or options could be attached to the debenture so that should the company go public or be bought out, an additional return could be earned for investors. Any one or combination of these sweetners would make the debentures more attractive to investors by exempting or deferring taxation for a period of time. The net effect of these features would be to increase the return to the holders without increasing the cost to the small business issuer.

To make the market in these debentures a secure and liquid investment, some measures of risk management and diversification would have to be incorporated into the issue. The small business loan secondary market could pool the debentures and diversify risk by issuing "Participation Certificates" similar to FNMA and Freddie Mac. Each individual investor would then be purchasing a small share in a larger number of small businesses thereby diversifying his/her risk. The secondary market could establish its own insurance fund to fund out losses in a manner similar to FHA. Alternatively, originators could be required to purchase equity in the secondary market intermediary similar to FNMA and Freddie Mac

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to cover debenture losses. The equity could be returned to the originators as the debentures were redeemed or repurchased.

The debentures would be structured to encourage the small businesses to repay the debentures in a timely fashion. The debentures should carry a term of five to ten years. The first five years, the non-diluting equity debenture would trade at par paying interest-only at some all-in rate such as prime + 2%. For each 20% reduction in the original borrowing, the interest rate would be reduced by (say) 3% for the next year. This "bonus" reduction in interest cost could not be passed onto investors. Similar to GNMA which incurs the discount cost on its special assistance function, the secondary market would have to make up the difference through some governmental appropriation.

J. CONCLUSIONS

In the national interest of creating jobs for future generations of Americans, small business growth needs to be encouraged and facilitated. The gaps in the capital markets discussed in this report are real and damaging. They place American enterprise in a serious disadvantage to other nations which can attract international (including American) capital because of their inexpensive cost of labor.

The proposals contained in this paper address only two of constrictions inhibiting successful small business development. The secondary market and non-diluting equity debentures do not offer the small business community any special advantages; they only remove from small business the obstacles others do not face. Correcting these imperfections in our capital markets will provide small businesses access to the same capital sources now open and available to the U.S. government, large multi-national investment overseas, and the individual homeowner.

The recommendations included in this report break little new ground. They simply outline ways in which we can apply time proven mechanisms for use in small business job creation. In the past, in the national interest of preserving a stable and liquid monetary system, a secondary market was created to permit the U.S. Treasury to borrow on a long-term fixed interest rate basis without jeopardizing the liquidity of our banking system. Historically, to permit large businesses to insulate their capital projects from the volatility of the credit markets, long-term, fixed interest rate debt has been offered through the secondary bond and equity markets such as the New York Stock and Bond Exchange. In the past, in the national interest of fostering a stable housing industry which provided adequate housing for all Americans, FNMA, GNMA and Freddie Mac were created. Now is the time to recognize that the future health of the American economy depends heavily on the ability of small businesses to grow and flourish. In our national interest, the creation of a small business loan secondary market and non-diluting equity debentures is warranted.

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Presentation to
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Emory University, August 4, 1986

PROMOTING SMALL BUSINESS EXPORTS

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The U.S. trade deficit in 1985 reached a record $148 billion. It is well on its way to exceed that level in 1986. The large inflow of imports without compensating exports is expected to hold 1986 GNP growth to about 2 percent. The need to increase U.S. exports is clear.

American small businesses played a key role in the recent economic recovery. They led the way in productivity and job creation, adding jobs at almost twice the rate of industries dominated by large firms.[2] The experience of small business exporters, however, sharply contrasts with those producing for and servicing the domestic economy.

Only one percent of U.S. corporations account for 80 percent of U.S. exports.[3] Although useful statistics are not gathered on the share of U.S. exports represented by small business, it is clear that they face special problems unknown to larger firms. Small business exporters have not nearly reached their export potential.

An area of particular interest to DSL has been small business export financing. In 1983, the Economic Development Administration, U.S. Department of Commerce, asked us to prepare a study, Export Financing for Small Business[4]. The two main conclusions of that study still hold true. One, export credit assistance programs are effective tools to increase small business exports. Two, for export credit systems to be effective, a credit delivery system is needed, designed to identify and attract small businesses who are currently exporting and have good potentials, and finally to secure the participation of regional and local banks.

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[1] I want to express my special thanks to Mr. Joseph Holtzman for his expert research and drafting assistance for this presentation.

[2] "The State of Small Business: A Report to the President", Washington, D.C., May 1985.

[3] Testimony of Kenn S. George, Director General, U.S. and Foreign Commercial Service, Department of Commerce, Hearing before the Subcommittee on Export Opportunities and Special Small Business Problems, of the Committee on Small Business, House of Representatives, Ninety-Ninth Congress, Washington, D.C., April 3, 1985.

[4] Domike, Arthur L., Ronald E. Muller and David Moore, Export Financing for Small Business, prepared for the Economic Development Administration, Department of Commerce, CITC, Washington, D.C. March 15, 1983.

Recent federal and state experience has confirmed these conclusions. The Small Business Administration (SBA), Export-Import Bank (EXIMBANK), Foreign Credit Insurance Association (FCIA) and the Department of Commerce, United States and Foreign Commercial Service (US&FCS), have all promoted small business exporters and export-capable firms through better targeting and coordination of services, and by seeking linkage with state programs.

State export promotion and financing programs have evolved to support and fill the gaps in federal programs. Although State-level experience varies, more and more states are providing such programs. We will look particularly at the experience of several states which have substantially increased their budgets and implemented innovative programs offering an extensive range of services.

In short, there has been progress in federal and state small business export programs since our 1983 study. But despite all, these programs have not yet had a major impact. There are 30,000 prospective small business exporters who are unserved, and only a handful of financial institutions are now actively engaged in export finance.

Two Major Problems

In line with the concern of the Commission with export opportunities and problems of small business, we would like to take this opportunity to present our view of what is needed to fill the gaps in federal and state programs to encourage more American small businesses to export.

We are mindful, as is the Commission, that trade barriers, protectionism, tax policies and similar problems inhibit trade expansion for both large and small companies. Our comments focus on the two major inhibitions of particular concern to small business exporters:

- the lack of low-cost, easily accessible export financing; and,
- the lack of flexible, well administered outreach programs and delivery systems which target participation of small business exporters and banks.

The Need for Additional Export Financing

The importance of low-cost export financing for promoting small businesses cannot be underestimated. In our Department of Commerce study we found that small business exporters experienced an absolute decline of 15 percent in real exports between 1980 and 1982, compared with a decline of only 8 percent for total U.S. exports over the same period. Our survey of 240 small business exporters showed that better financing alone could have improved their export performance by over 50 percent. Other evidence abounds:

- Only one percent of SBA's loans in 1983 were for exports, totalling 51 loans for $14.1 million. This rose slightly in 1984 to a total of 65 loans for $15.9 million, and in 1985 to a total of 62 loans for $16.7 million. No export loans have yet been made in FY 1986.[5] Included in these figures are all SBA revolving credits for export, as well as loans under the new joint financing arrangement between SBA and EXIMBANK;

- The Third World debt crisis led almost all regional and local banks to withdraw from international lending, including even short-term suppliers credits. EXIMBANK, SBA and state loan guarantee programs have not provided adequate inducements for these banks to assist small business exports;

- Tax reform threatens other remaining sources of small business financing, particularly by elimination of Small Issue Industrial Development Bonds (SIDBs). About two out of five Small Issue users are engaged in export trade and have used their Small Issue financing for trade related projects. Two-thirds of these trade impacted projects are in the manufacturing sector, and fully half of all manufacturing projects aided by Small Issue bonds produce some portion of their output for export;[6]

- Only 10 states have operational export financing programs, 7 of which also provide export insurance. Two of these states have loans-to-lenders programs, as do 4 additional states. (See Table 1).

International developments have also made urgent the need for additional small business export financing. Despite the recovery in much of the U.S. economy, many small business export industries were hit hard by the 1981-83 recession, and have not recovered their former export markets. Machine tools is a prime example. Traditional export markets in Europe, OPEC and Latin American countries were lost to competition during the epoch of the strong dollar and the continued slow growth of those economies. The decline in interest rates and the value of the dollar have certainly not had the benefits for exports that were so widely predicted.

Table 2 illustrates the changing importance of selected international markets to U.S. small business. The high value of the dollar played a significant role in the declining competitiveness of U.S. products in the Canadian and English markets. In Mexico and South America, the reduced ability to import due to the debt crisis, combined with the higher cost of

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[5] Interview with Mr. Julius Toma, Export Financing Program, Small Business Administration, July 15, 1986.

[6] DSL Consortium, Small Issue Industrial Development Bonds and the U.S. Economy, Council of Industrial Development Bond Issuers, Washington, D.C., March 1986.

TABLE 1

STATE EXPORT FINANCE PROGRAMS

State	Type of Authority (a)	Date Operational	Funding Level(b) (In $millions)	Funding Source	Program Characteristics: Loan Guarantees	Loans to Leanders	Insurance	Counseling
California	A	1985	2.0	appropriation	x		x	x
Colorado	B	(c)	0.0	---	x		x	x
Illinois	A	1985	100.0	bonds	x	x	x	x
Indiana	B	1983	4.0	appropriation	x			
Louisiana	A	(d)	50.0	bonds-		x		
Michigan	B	1984	10.0	bonds		x		
Minnesota	A	1983	2.0	appropriation	x		x	x
Mississippi	B	1984	1.0	earmarked funds	x			
Missouri	B	1984	1.6	appropriation	x			
Ohio	B	1983	100.0	earmarked funds		(e)		
South Carolina	A	(d)	100.0	bonds	x	x	x	x
Tennessee	A	(c)	0.0	bonds	x		x	x
Washington	A	1983	(f)	(f)				x
West Virginia	A	1985	50.0	bonds	x		x	x
Wisconsin	B	1983	50.0	bonds		x		

(a) A = Creation of a new export finance authority, either as a separate entity or as a new office within an existing department. B = Expansion of the responsibilities of existing agencies.

(b) These figures are for program levels and do not include funds for operation and administration.

(c) No money has been appropriated or designated; agency offers only minimal counseling services.

(d) Questions still remain regarding the tax-exempt nature of the bond issues.

(e) Ohio's program is known as a "linked deposit" program. Using existing state funds, the state deposits money which the bank then lends to a qualified small business at below market rates. This is a variation on the loan-to-lender approach.

(f) Washington's program is prohibited from using state funds for loans and loan guarantees. The state can accept federal funds or sign a contract with a state development agency to furnish these services.

Source: States in The International Economy, Committee on International Trade and Foreign Relations National Governors' association, August 4-6, 1985.

U.S. products resulted in a sharp drop in U.S. exports to those countries. Between 1982 and 1985, Mexico's market share of U.S. small business exports declined from 8.1 percent to 1.8 percent of the total U.S. small business exports. Small business export markets exhibited relative growth only in Asia, where the currencies of many countries -- such as Taiwan and Korea-- are tied to the U.S. dollar.

TABLE 2

CHANGES IN SELECTED MARKETS FOR U.S. SMALL BUSINESS MANUFACTURED EXPORTS

(Percent of Total Exports)

Market	1979	1982	1985
Canada	23.7	18.1	15.7
England	8.6	7.4	6.4
Asia	12.4	13.9	16.2
Mexico	5.9	8.1	1.8
South America	8.6	6.8	4.1
Total, Selected Markets	**59.2**	**54.3**	**44.2**

SOURCE:Survey data of the National Center for Export-Import Studies, cited in Prepared Statement of Dr. Michael Czinkota, Chairman, National Center of Export-Import Studies, Hearings before the Subcommittee on General Oversight and the Economy, of the Committee on Small Business, House of Representatives, Ninety-ninth Congress, Washington, D.C., June 25, 1985; and Frederick, Md., September 16, 1985.

Small business export financing is important as a generator of high quality private sector employment. DSL found that small business export stimulation through special financing programs is a better way to generate employment than all the alternative policy options examined, including financing programs for all manufactured exports, personal and corporate tax cuts, and a general increase in defense purchases.[7]

Relatively small volumes and values of individual transactions mean that small businesses often have fewer credit options and face higher transaction costs, including such costs as credit checks. Few small business exporters can float commercial paper and must, in effect, pledge their business assets to gain any credit.

Small business exporters especially need two kinds of financing:

- Pre-export working capital to cover input acquisition, processing and shipment is their most pressing capital requirement,

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[7] See, Export Financing for Small Business.

- Export receivables finance for small business to match U.S. and overseas competition which allow most purchasers to delay payment for up to six months. The exporter usually carries this cost, fully exposed to the payment risks and delays.

There are federal export credit programs at SBA, EXIMBANK and Federal Credit Insurance Association (FCIA). But -- as the House Committee on Small Business noted --

> None really exist in significant amounts to make funding available for the short-term transactions that constitute the major kind of export sale made by small exporters and which also account for large proportion of sales made by medium-sized exporters.[8]

A short-term loan guarantee program for both working capital and export receivables would be of particular help to small business exporters. By increasing their access to short-term credit, small business exporters would have a strengthened capability to respond to new export opportunities. This program could be self financing and initially funded by either the federal government, individual states, or through some mixed federal/state funding formula. The important thing is that the program be administered through local banks with the State agency to ensure easy participation by small business exporters and allow an on-going relationship between the agency bank and small business.

Also important is to make available to small businesses financing at the lowest cost. Some states capitalize their export finance funds through legislated appropriations. Others, such as Illinois, have tapped the bond markets to ensure the availability of interest rates and borrowing costs lower than normal costs of a commercial loan.

Because all states which could benefit from such a program may not have the financial and/or staff ability to initiate and service such a program, we recommend that the program be established by EXIMBANK and administered locally through state agencies. The agency would be authorized to utilize EXIMBANK loan guarantees, thus allowing greater flexibility to customize the assistance the participant's needs. A second-best approach, and the more feasible, is for individual states to establish their own programs. Some states have adequate staff to conduct outreach and financing programs. Others do not and will need to contract-out those tasks. For this latter group, it is important that they recognize this need and plan for it.

This proposed guarantee program for short term credits would cover the following:

- Pre-export working capital for up to 50 percent of input costs would be offered for 90 days, with total credits not to exceed $2 million per firm.

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[8] State, Local and Private Sector Small Business Export Initiatives, a Report of the Committee on Small Business, House of Representatives, Ninety-Eighth Congress, G.P.O., Washington, D.C., September 18, 1984., p. 17.

- Financing guarantees would be provided for up to 65 percent of export receivables, at market rates for 180 days. Commercial banks would dispense the loans and assume the unguaranteed portion (35 percent).

We want to emphasize that such a program has modest risk and expenditure requirements, but can have significant benefits and export additionality. It can be designed to be self-financing, so as not to require new government appropriations even while generating new exports, new employment, GNP growth and new federal and state revenues. The key here is new exports, those of both existing small business exporters and new-to-export firms, so that there is both greater additionality and economic multipliers.[9]

We recommend that the short-term credit guarantee program include criteria for assuring that roughly half of all transactions within 3 years of program implementation involve firms which are new to export, new to a particular export market, or are marketing a new product. The quantitive goal should be flexible in order to also have the program counteract downturns in the business cycle and/or international trade growth. It may be preferable to sacrifice some additionality in the initial period, while firms become acquainted with the facility. This would reduce administrative confusion and encourage a larger client base in the near-term. In addition, the unguaranteed portion assumed by the participating bank or financial institution could begin at 10 percent, rising to 35 percent within three years. Reducing these risks in the near-term should encourage participation of smaller local banks which are new to the international market.

Costs and Fees

We estimate that only 15-20 percent of the exports covered by state programs would need to be additional or new exports for the loan guarantee program to cover its costs.[10] We want to emphasize that access to the program by the prospective small business exporter is affected by both the fee amount and fee schedule. We specifically recommend that the fee structure be designed along the lines of other export credit programs of OECD rather than that of EXIMBANK. The EXIMBANK charges only a 2 percent fee -- which is lower than other OECD programs -- but the fee is a serious burden to small business because it must be paid up-front as an application fee. Program participation is thus restricted for small business exporters who are vulnerable to cash flow shortages. In other OECD export credit programs, the fee may be financed over the life of the loan, reducing the up-front cash burden.

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[9] If the proposed financing program were to simply replace existing credits without adding to exports, there would be no "additionality" nor multiplier. As discussed below, the program must be designed to avoid this.

[10] See, Export Financing for Small Business. p. 75.

Export Development Programs

Although everyone agrees that an important objective of new export promotion efforts and financing programs is to increase small business exports, federal and state officials are still grappling with the "how-to" of effective export inducement.

Several recent state export promotion efforts are most encouraging reflecting a broadened appreciation of the importance of small business exports, and recognition that they can fill special niches in key industries which are still dominated by small business, such as machine tools, specialty electronics, chemicals and pharmaceuticals. Firms such as these need special support services if export potentials are to be realized.

The experience of the export development programs is very uneven between states (See Tables 3 & 4). The most sophisticated states, such as Washington, have full time professional staff and a computerized delivery system for financial counseling services. Minnesota is establishing "one-stop" offices for export and other trade assistance. Most other states, however, have limited staffs and budgets and serve largely as a referral service. It is these states that can most benefit from the advanced experience of such states as Illinois, Minnesota and Washington. However, a national mechanism to synthesize and disseminate such information does not currently exist. (see below, "Monitoring and Evaluating System")

Table 3

STATE EXPORT PROMOTION SERVICES AND PROGRAMS

Service		No. of States With Service
1.	Seminars/Conference	49
2.	Sales leads dissemination	45
3.	One-on-one counseling	43
4.	Trade shows	40
5.	Trade missions	39
6.	Referrals to local export services	31
7.	Foreign office representation	30
8.	How-to handbook	24
9.	Market study preparation	23
10.	Newsletters	23
11.	Language bank	13
12.	Operational Export Finance Program	10

Source: National Association of State Development Agencies (NASDA) and National Governor's Association (NGA), in, STATES IN THE INTERNATIONAL ECONOMY, Committee on Trade and Foreign Relations, National Governors Association, August 1985.

TABLE 4

State Foreign-Trade Development Programs

	Seminars/ conferences	One-on-one counselling	Market studies prepared	Language bank	Referrals to local export services	Newsletters	How-to handbook	Sales leads disseminated	Trade shows	Trade missions	Foreign office reps	Operational financing program
Alabama	●	●			●		●	●	●	●	●	
Alaska	●	●	●	●			●	●	●	●	●	
Arizona	●	●	●			●		●	●	●		
Arkansas	●	●	●	●	●	●		●	●	●	●	
California	●	●		●		●	●	●	●	●		●
Colorado	●	●	●		●			●	●	●		
Connecticut	●	●	●		●	●		●	●		●	
Delaware	●				●			●	●			
Florida	●	●	●		●	●		●	●	●	●	
Georgia	●	●	●		●			●	●	●	●	
Hawaii	●	●			●			●	●	●		
Idaho	●							●	●	●		
Illinois	●	●	●		●			●	●	●	●	●
Indiana	●	●		●				●	●	●	●	●
Iowa	●	●	●	●			●	●	●	●	●	
Kansas	●	●		●	●	●	●	●	●	●	●	
Kentucky	●	●			●		●	●	●	●	●	
Louisiana*	●	●			●	●	●	●	●	●		
Maine	●							●		●		
Maryland	●	●				●		●		●	●	
Massachusetts	●	●	●		●				●	●	●	
Michigan	●	●	●			●	●	●	●	●	●	●
Minnesota	●	●			●	●		●	●	●	●	●
Mississippi	●	●	●		●	●	●	●	●	●		●
Missouri	●	●	●		●	●	●	●	●	●	●	●
Montana	●	●	●		●		●	●	●	●		
Nebraska	●	●		●	●		●	●	●			
Nevada	●			●		●				●		
New Hampshire	●	●			●		●	●				
New Jersey	●	●			●	●		●	●	●		
New Mexico	●	●			●		●	●			●	
New York	●	●			●	●	●	●	●	●	●	
North Carolina	●	●	●	●	●	●		●	●	●	●	
North Dakota	●	●						●	●			
Ohio	●	●	●	●	●	●		●	●	●	●	●
Oklahoma	●	●	●	●	●	●	●	●	●	●		
Oregon	●	●				●	●	●	●			
Pennsylvania	●	●	●		●	●	●	●	●		●	
Rhode Island	●	●			●	●	●	●	●	●	●	
South Carolina	●	●	●		●			●	●	●	●	
South Dakota	●	●	●	●				●				
Tennessee	●	●	●		●		●	●	●	●		
Texas	●	●					●	●	●		●	
Utah	●	●					●	●	●	●	●	
Vermont	●										●	
Virginia	●	●	●					●		●	●	
Washington	●	●	●	●	●	●	●	●	●	●	●	●
West Virginia	●									●	●	
Wisconsin	●	●			●	●	●	●	●	●	●	●
Wyoming										●		
Totals	49	43	23	13	31	23	24	45	40	39	30	10

Source: NASDA, [illegible] in Business America, May 27, 1985 (updated [illegible] Committee staff)

Most state export development programs have expanded slowly. Only 10 states have operational export financing programs and three of them were implemented only in 1985. In addition, several of the state financing programs started as local delivery systems for federal programs and procedures. Looked at positively, this approach can build on evaluations of programs and bring measured responses to identified problems. The negative side is that it may yield a piece-meal approach to small business export promotion with unclear objectives and tasks.

We want to emphazise that the initiation of state export financing programs should have clearly defined objectives for international trade and marketing strategies, based on the special economic and social characteristics and needs of individual states. For those states without operational financing programs, it would not be appropriate to establish export financing programs without having such a strategy, including an accurate estimate of the demand for such financing.

Export Finance Programs and Managerial Time

Federal export financing programs provide important experience from which to draw conclusions about most needed initiatives. Our work shows the following as the major problems with most federal and state export financing programs:

- Poor or non-existent systems to identify potential small business exporters and local/regional banks to participate in the export financing program, and
- Lack of integrated services which increase the attractiveness of participation for both small business exporters and banks by effectively reducing the managerial time and cost of participation.

Many studies have identified "lack of information" as a key obstacle to small business exporting. We agree. But the problem is not a lack of data or publicity folders. Federal and state programs have produced bushels of publications about small business exporting and overseas markets which are generally good and easily understandable. However, only the intrepid and unhurried entrepreneurs who walk through the agency door generally receive this information. There is a need to increase small business awareness and utilization of existing programs in general, and particularly target those potential exporters who currently do not. However, even if more small business exporters are brought into the programs, their financing needs will not be met unless local/regional bank participation is also secured.

The key to both identifying and attracting new small business and local/regional bank participants is a comprehensive state program or a state-level delivery system for federal programs. The need is the same for all states, regardless of their present program development.

One-Stop Shopping

The multidisciplinary approach creates a system for assuring that prospective small business exporters receive the information, counseling and technical assistance required to understand the export and financing process, and to prepare all of the documentation necessary to show their creditworthiness before approaching the banks. This approach minimizes the demand on managerial time of both small business and local/regional bank executives.

The need for one-stop export financing and trade promotion services for the small business exporter becomes apparent when we look at the practice of the largest source of export and trade counseling, and overseas market information -- The United States & Foreign Commercial Services (US&FCS).

According to its Director General, US&FCS is "the home for small and medium size business when it comes to international trade."[11] The counseling and information services provided by the agency are indeed extensive. Confidential issues are addressed involving business product secrets, economics, marketing strategies and plans for entering the international market. These sessions take a serious time commitment by the potential small business exporter. However, at the end of the counseling, when the need for export financing is identified, the US&FCS counselor directs the potential exporter elsewhere.

If the objective of the US&FCS is to encourage small business exports, it is clearly counterproductive to force the prospective exporter to shop around for a bank willing either to provide export financing on its own or to participate in a federal or state program. Delays and lost time mean lost export opportunities, if only because the firm has to repeat the time consuming "get acquainted" period with new bank, federal and/or state officials.

Although we do not expect US&FCS to add an export financing facility, state programs can benefit from this experience by combining counseling and financing facilities. The counselor with extensive knowledge of a firm's condition and plans should be able to help the company secure export financing. This may also encourage private local/regional bank participation in the federal or state credit guarantee program.

Another type of one-stop shopping for export development and financing services is currently being implemented by the Minnesota Trade Office, comprised of five divisions: 1) International division; 2) export counseling services; 3) agricultural exports; 4) communications/marketing; and 5) export financing authority. All of these services will be housed in the Minnesota World Trade Center, currently under construction.

Together, the five divisions of the Minnesota Trade Office provide a comprehensive range of small business export counseling, technical and financing services. (See annex A)

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[11] Testimony of Kenn S. George, Director General, US&FCS, April 1985.

Inducing Bank Participation

EXIMBANK, SBA and State loan guarantees have not provided the necessary incentives to encourage local/regional bank participation in export financing. In its annual survey of representative banks and exporters, EXIMBANK notes that banks are most concerned with processing time and paperwork requirements. Local/regional banks already view any type of small business financing as risky and a waste of bureaucratic time. Their risk perception only becomes greater when they are thrust into current problems and uncertainty of the international economy -- particularly of the developing countries which are a significant unexploited market for small business exporters.

It should be obvious that when a small business borrower approaches a bank with incomplete documentation and near-total ignorance of the export and financing process, he/she will be summarily turned down regardless of the international competitiveness of the product. The small amounts of financing required by the small business exporter are inevitably insufficient to justify the time costs of the counseling that the bank would have to provide. This problem is compounded by the additional paperwork and time associated with bank participation in federal and state export financing programs.

Greater local/regional bank participation in federal and state export financing programs must, therefore, be designed:

- to minimize the amount of time and risk required to service small business exporters; and,
- hold out the prospect for on-going business and higher levels of borrowing.

Its not enough to hold educational seminars for small business exporters, although these should be used. Rather, the firms need access to an integrated package of services so they can walk into a bank with financials and paperwork completed, with a clear understanding of the company's market strategy, mode of shipment and method of payment options, U.S. export licensing regulations and foreign import restrictions in the market destination. From the bank's viewpoint, this customer would be highly attractive because he /she would only require financing. From the small business exporter's viewpoint, this would minimize time and frustrations involved in securing bank financing. The probability of greater program participation and increased exports showed result.

The Illinois Export Development Authority is an example of a program designed to limit paperwork and the time commitment required of participant banks and small business exporters. The Authority will initiate, prepare and process the documentation and insurance needed to qualify the Illinois exporter and its foreign buyer. This is particularly helpful to those banks that want to expand into the international market, but do not have in-house, the knowledgeable personnel or division to handle the paperwork. (See Annex B).

Another important aspect of the Illinois export financing program worth mentioning is bank participation. The Illinois sale of Export Development Revenue Bonds to finance its new small business export loan program was guaranteed by a letter of credit (LOC) issued by The Bank of Tokyo, Ltd. This is part of the aggressive role being played by Japanese banks in areas of state and local economic development financing. Japanese banks have stepped into the gap left by U.S. banks unwilling or unable to hold on to this market.

In a composite issuance of small issue industrial development bonds by the Industrial Development Authority of the County of Los Angeles, which DSL designed, the Dai-Ichi Kangyo Bank, Ltd. provided the letter of credit. If U.S. banks do not actively compete for the market provided by state and local economic development and export financing programs, they will simply lose out to the Japanese and other foreign banks willing and eager to participate.

A Monitoring and Evaluation System

Because the states have different experience, characteristics and needs, the most important weaknesses and policy prescriptions will be different. A system is needed to evaluate the experience of all state export promotion programs in order to replicate their achievements and avoid creating new pitfalls. The National Association of State Development Agencies (NASDA) and the Committee on International Trade and Foreign Relations of the National Governor's Association (NGA) presently monitor the practices of state export promotion programs. We believe this effort could be strengthened by a well targeted analysis on a national scale of the work of state export agencies. These associations could take the lead in conducting the studies and keeping them updated.

A coordinated study would help states and federal agencies to determine ways to spur program effectiveness in promoting exports and/or job creation, and to identify necessary program changes and/or additions. A data base to allow a social cost-benefit and cost effectiveness evaluation of the export promotion programs would be developed by monitoring and collecting information from ongoing programs. The data bases would include:

- new exports created by each program;
- economic impacts of program activities, especially job and tax revenue generation;
- volume and types of transactions and exports;
- transaction costs;
- regional and industry distribution of program activities and economic impacts;
- personnel skills and the quality and quantity of technical assistance, and;

- the quality and cost of promotional literature and activities.

The organizational infrastructure of the export promotion programs should also be part of on-going monitoring and evaluation. The ability to fit the varied needs and procedures and coordinate program relations with the state government, large and small exporters, large and small banks and private financial institutions, federal export development programs at EXIMBANK, SBA, FICA and US&FCS needs to be examined.

States do not have to wait for a national study or the lead of federal agencies. They should themselves monitor and evaluate their small business export promotion programs. This will be of direct benefit to the state, and also facilitate regional initiatives and cooperative arrangements to share useful information and increase the available export opportunities.

Conclusion

States and federal agencies are increasing their efforts to encourage small business exports. The experience is varied, but holds many lessons which must be systematized, popularized and adapted to differing needs and objectives at the state-level. However the following proposals apply to all or most states:

- Design and implement an international trade promotion strategy based on the characteristics and economic development needs of each state.

- **Small Business Exporters.** Stimulate small business participation in state export development programs by providing low-cost financing and the full range of technical assistance, trade promotion, marketing and financial services to streamline the export process, reduce managerial time and costs, and strengthen small business ability to quickly respond to, and benefit from, new export opportunities;

- **Local and Regional Banks.** Stimulate local/regional bank participation in state export financing programs by minimizing the bank's risk and amount of time required to service small business exporters, through a combination of loan-to-lender, loan guarantee and insurance programs. Also assure bank participants that on-going participation will entail higher, total levels of borrowing.

- **Short-term Export Finance.** This program addresses the short-term credit gap faced by many small business exporters. An on-going loan guarantee program would combine export **receivables** and **pre-export working capital financing.** Strict participation criteria would be set to guarantee high additionality regarding new exports which would not have been made without the State financing program The guarantee fund would be capitalized through a bond sale in the capital markets in order to reduce the cost of funds to the exporter. The state agency would initiate and process the paperwork. Local banks or financial institutions would disseminate the loans.

o **Monitoring and Evaluation System.** A national, state-based system is needed to evaluate the experience of all state exports promotion and financing programs in order to replicate their achievements avoid creating new pitfalls. A coordinated study and effort would help states and federal agencies to determine ways to spur program efficiency in promoting exports and/or job creation.

APPENDIX A

THE MINNESOTA TRADE OFFICE

The Minnesota Trade Office was established in July 1983 and has become a one-stop shopping center for all export-related information, counseling and technical assistance and finance.

Within the Trade Office are five divisions: 1) Export services; 2) Agricultural exports; 3) Communications; 4) International division; and 5) Export Finance Authority. A World Trade Center is currently under construction in St. Paul which will house all of these services and programs and provide a site for trade shows and missions.

As a one-stop center, the Minnesota Trade Office is unique. Small business exporters and export-capable firms have a full range of services in one place, eliminating the bureaucratic running around required of most states and federal agencies and programs. For the small business with little extra-available time and/or personnel, the one-stop center is a major attraction which should encourage greater participation.

The Minnesota Export Finance Authority (MEFA) is also unique. It was the first state agency of its kind. One program is a pre-export loan guarantee program to provide working capital for the small business exporter. Each company is limited to $250,000.

Since July 1, 1984, the Minnesota Export Finance Authority has guaranteed 14 loans for a total of $1.4 million. There have been no losses to date.[1]

In order to qualify for the pre-export loan program, a small business must meet three requirements:

1) The company needs a bonafide purchase order of sales contract;

2) The company must be refused alternative credit from a bank; and,

3) The company must obtain a letter of credit, to guarantee the MEFA program loan.

In February 1986, MEFA co-guaranteed with EXIMBANK a working capital loan for $500,000. This was the first such co-guarantee arrangement between EXIMBANK and a state agency, implementation of which needs to be expanded.

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[1] Interviews with Mr. Devon Rice, Minnesota Export Finance Authority, July 30, 1986.

The Minnesota Export Finance Authority also provides political and commercial risk insurance through the "umbrella program" with the Foreign Credit Insurance Association (FCIA) and EXIMBANK. For an exporter to qualify for the Umbrella program, it must be a small business with total export sales of $2 million. This includes export sales of all corporate affiliates.

The application process for the Umbrella insurance program is purposely short, consisting of a one page form. Although all approvals must be made by FCIA in New York, turnaround time is usually 1-2 weeks. Payout is guaranteed within 30 days of a claim.

The umbrella program is designed to stimulate new exports. Unlike federal and state programs which provide a general line of credit, the Minnesota program only considers the individual transaction. Small business eligibility is therefore not restricted solely based on its balance sheet and general credit relationship with a bank. MEFA looks beyond the balance sheet at the individual transaction to approve the firm and foreign buyer. MEFA also structures the Transaction with a letter of credit on insurance, reducing borrower and bank risks.

With a staff of 35 people and large budget, the Minnesota Trade Office is able to provide extensive services to the small business exporter. Some of these programs have been quite innovative and should serve as a model for other state export development programs. However, program results to date have be[illegible]d.

State officials have acknowledged that the trade office must better market its programs. The monthly seminars held for bankers and exporters on how to finance exports and use State and federal programs are not enough to stimulate greater participation in the programs. The one-stop center offers great pote[illegible] But it may be necessary to better target and survey small business[illegible] and banks in the state to motivate new exports.

APPENDIX B

THE ILLINOIS EXPORT DEVELOPMENT AUTHORITY

The State of Illinois has taken an active interest in promoting small business exports. In response to an identified need for small business export financing, the State recently established the Illinois Export Development Authority which operates out of the Office of the Lt. Governor.

The Illinois Export Development Authority (IEDA) export loan program is unique in several ways:

- o IEDA pre-qualifies potential bank and small business participants;
- o IEDA completes most of the documentation and paperwork for both the exporter and lending bank;
- o IEDA provides both less costly and larger loans previously unavailable to small business exports, by tapping the capital markets through its Export Development Revenue Bonds, which are taxable by the federal government, but tax-exempt with regard to the State.
- o Small business export loans are available, easily and quickly through a company's local bank or financial institution.
- o Banks can participate with very low risk and can enter the international trade market without a large personnel commitment A small company's regular loan officer can also service the IEDA export loan.

IEDA only recently capitalized its export loan fund through the issuance and sale of $15 million of Export Development Revenue Bonds in early July, with a limit of $100 million. The initial $15 million issue was determined through a survey to assess near-term demand for small business export financing.

The Bank of Tokyo, Ltd., issued the letter of credit (LOC) to guarantee the bonds. The Bank also created a formula with financial eligibility criteria to help pre-quality participating banks. IEDA pre-qualified small business exports, so that a surveyed and pre-qualified list of companies and banks are waiting to participate The Bank of Tokyo is both guarantor of the issued bonds and a qualified lender of the IEDA program.

The IEDA export loan program extends a line of credit to participating banks, which in turn provide an export financing loan to the small business exporter. IEDA funds 90 percent of the loan, with the participating bank providing 10 percent. Each loan must be insurable against political and commercial risk through the Federal Credit Insurance Association (FCIA).

The insurance of the loan has two advantages:

- For the small business exporter, the only collateral required for the loan is the contract or receivable generated by the sale, leaving other assets intact for other credit purposes;
- For the bank, insurance eliminates almost all loan risks.

The IEDA export loan program provides both pre-export working capital to fulfill the sales contract and/or order, and to cover export receivables at a fixed rate for the life of the loan. Each small business exporter is limited to a maximum ceiling of $500,000 at a cost less than that available through traditional commercial financing sources.

Although the IEDA export loan program is targeted at small businesses that are ready to export, the Authority's survey and promotion activities have also reached export capable firms which currently do not export their products. For these latter firms, marketing and technical assistance are needed to introduce and prepare them for the export process. These activities are conducted through the Small Business Assistance Bureau, Illinois Department of Commerce and Community Affairs.

The IEDA small business export loan program has yet to make any loans, but both companies and banks are waiting to participate. The appeal of the program is reflected in the increasing number of small business and bank inquiries. A major attraction of the program is the limited paperwork requirements. The paperwork and documentation is limited to a 3 page application form, a letter from the small business requesting to participate in the program and a financial statement. In addition, the Illinois Export Development Authority will initiate and process the paperwork to qualify the exporter and its foreign buyer for insurance and will prepare the documentation thereby relieving the exporter and lending bank from this costly time requirement.

MAKING AMERICA WORK AGAIN

Jobs, Small Business, And The International Challenge

The National
Commission On
Jobs And
Small Business

Making America Work Again

Jobs, Small Business, And The International Challenge

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Preface

Few areas of our national life are as important to our economic health and well-being as small business. Small enterprises represent the economic backbone of communities across the country, the major source of job creation in the United States, and a vital source of the innovation, new products, and services which drive our economy.

These reasons alone were sufficient for each of us to agree to serve as co-chairs of the National Commission on Jobs and Small Business when it was convened in September 1985 by eighteen leaders of the United States Senate and House of Representatives.

Each of us had, in addition, a more personal interest in the success of this significant undertaking. One of us started his career in private life by establishing, in the rural South, a small firm which became an important part of the local economy and earned in its first year exactly $187. The other, as a member of the House of Representatives for many years, represented a midwestern city whose small firms were the foundation of the manufacturing, supply, and distribution systems for the American automobile and furniture industries.

Far from a national abstraction, small business to each of us represents the very heart of economic opportunity in America and a linchpin of our social and economic cohesion.

The Commission has completed its important work, and the conclusions and recommendations in this report deserve the attention of citizens everywhere. Our hope is that the report will help trigger the renaissance of entrepreneurship and business creation needed to carry America successfully into the 21st century.

Jimmy Carter Gerald R. Ford

Jimmy Carter
Plains, Georgia

Gerald R. Ford
Rancho Mirage, California

Members of the National Commission on Jobs and Small Business

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Honorary Co-Chairman

Gerald R. Ford
Honorary Co-Chairman

Sam Beard (Chairman)
Wilmington, Delaware
Chairman
National Development Council

Bernard E. Anderson
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Senior Economist
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Murray Hill, New Jersey
Chairman (Retired)
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American Enterprise Institute

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Robert Woodward
Atlanta, Georgia
Partner
King & Spalding

James J. Harvey
Executive Director

Congressional Conveners

The Commission was convened on September 10, 1985 by the 18 members of the U.S. Senate and House of Representatives who had urged its establishment. The conveners, representing many of the major committees in the Congress, all regions of the country, and both parties, include:

U.S. Senate

Sen. Lloyd Bentsen
Committee on Finance

Sen. Alfonse M. D'Amato
Committee on Banking, Housing, and Urban Affairs

Sen. Alan J. Dixon
Committee on Small Business

Sen. Slade Gorton
Committee on the Budget

Sen. Sam Nunn
Committee on Small Business

Sen. Warren Rudman
Committee on Appropriations

House of Representatives

Rep. Berkley Bedell
Committee on Small Business

Rep. Lindy Boggs
Committee on Appropriations

Rep. Rodney Chandler
Committee on Science and Technology

Rep. Augustus F. Hawkins
Committee on Education and Labor

Rep. James M. Jeffords
Committee on Education and Labor

Rep. John J. LaFalce
Committee on Banking, Housing, and Urban Affairs

Rep. Trent Lott
Committee on Rules

Rep. Lynn Martin
Committee on the Budget

Rep. Joseph M. McDade
Committee on Small Business

Rep. Parren J. Mitchell
Committee on Small Business

Rep. Henry J. Nowak
Committee on Small Business

Rep. Ed Zschau
High Technology Task Force

Foundation Support

Major support for the Commission was provided by the Charles Stewart Mott Foundation, Flint, Michigan. Other substantial support included:

The Carnegie Corporation of New York (through the Carnegie Forum on Education and the Economy)

The John D. and Catherine T. MacArthur Foundation, Chicago, Illinois

The Andrew W. Mellon Foundation, New York, New York

The National Development Council, New York, New York

The Rockefeller Foundation, New York, New York

Introduction

In September 1985, a bipartisan coalition of members of the House of Representatives and the Senate of the United States established the National Commission on Jobs and Small Business and charged it with recommending policies to create 10,000,000 new jobs through small business.

It has been my privilege to chair this endeavor, and, on behalf of the members of the Commission, it is my pleasure to transmit this report, *Making America Work Again: Jobs, Small Business, and the International Challenge*, to the 100th Congress of the United States.

Our job creation goal required us to define the problems of American workers and small business owners in a period of dramatic economic change. The candid and vigorous deliberations of the Commission concentrated the search for solutions on the conditions which nurture enterprise and, in that context, on what the country needs to do to encourage small business formation, a more secure environment for workers, and economic growth.

When the Commission first met, President Reagan spoke of the invaluable economic contributions of the small business owner when he said, "Free enterprise and entrepreneurship are the roots of a healthy economy." This report builds on that insight.

In going about its work, the Commission relied on several sources of information: papers commissioned from experts on a variety of business, economic, and education issues; surveys of small business owners and corporate chief executive officers; eight intensive hearings around the country on a variety of issues affecting small firms; existing analyses of problems in American business from several public and private sources; and the debates, papers, and resolutions prepared for the 1986 White House Conference on Small Business.

During 15 months of study and investigation, the Commission heard from the leaders of the small business community, from delegates to the White House Conference, from members of Congress and the executive branch, from state and local officials, from executives, academic, financial, and corporate leaders, and from the people whom small businesses employ.

We heard from several of the owners of America's 15 million small firms. By nearly any measure they represent a formidable economic force. They employ nearly half of the private non-farm workforce in America, and produce 47 percent of the country's gross domestic product.

We were impressed with the diversity of their opinions as well as with the sense of optimism which characterizes their attitude toward American business life. The members of the Commission mirror that diversity and optimism for the future despite our concern with the enormous economic changes that threaten our people's standard of living unless the country attends to them now.

A complete list of all those who helped make this undertaking possible is included in the appendices which complete this volume. We are, in particular, grateful to those witnesses who took the time, often at their own expense, to provide us with the benefit of their experience. In all cases, the Commission has taken their views into account even if the conclusions in this report differ from their suggestions.

A special word of appreciation is due the four Congressional leaders who planned the announcement of the Commission's establishment—Senators Sam Nunn (Georgia) and Slade Gorton (Washington) and Representatives Parren J. Mitchell (Maryland) and Lynn Martin (Illinois). Without their assistance, our efforts would have been considerably more difficult.

I must also express my admiration for the members of the Commission. Each devoted long hours and days, without compensation, to this work. As a group, the Commissioners brought to this undertaking not only their energy and the experience of their diverse backgrounds, but also a commitment to the public interest, to small business, and to our goal of creating ten million jobs. Their skill, intelligence, and good humor throughout our investigation made it succeed; their willingness to accommodate the diversity of opinion on the Commission made this report possible. Each Commissioner would probably have written a somewhat different report, but all were in agreement with the central messages of *Making America Work Again*.

The Commissioners join me in thanking the members of the staff for their energetic organization of our activities. Particular thanks are due to James J. Harvey, executive director of the Commission, for his contributions to our work and for his assistance in drafting this report.

Finally, the Commission acknowledges the debt it owes to William S. White, president of the Charles Stewart Mott Foundation, Flint, Michigan. His vision of the need for the Commission sustained us in the months of planning, and his support during our tenure made this report possible.

Sam Beard

Sam Beard
Chairman

The American people need to be clear about the significance of the American promise. It represents far more than a platitude. At the core of the promise is our national affirmation of the dignity of the individual. The pledge that all can create their own destinies holds a powerful appeal to people around the world and is . . . the foundation of our national economic growth. That promise animates and sustains small business.

Now the legacy is itself imperiled.

It is time America came to its senses. Wishful thinking and dated views about our place in the world have obscured the domestic effects of international economic competition. Because each generation of Americans has exceeded the standards of its parents in health, income, education, and material well-being, we have long taken our prosperity for granted. But now, a new prospect emerges: for the first time in recent history, our children's standard of living may not equal, much less exceed, our own.

The outlook for the next generation is troubling. Our country is unable to sell many of its products at competitive prices on world markets. Too many of our people are unemployed or underemployed. Several of our great industries are in trouble. Even our advantages in technology and agriculture are fading rapidly. Our ability to meet our obligations as a world leader is threatened by the erosion of the nation's competitive position in commerce, industry, and technology.

Our society seems to have forgotten one of the important truths on which it was founded: in a democracy it is not the government that creates wealth, but the people and their belief in themselves. Adrift from that mooring, we have lost sight of the commitment and hard work critical to maintaining our international standing. We have forgotten also that just as individual rights are the foundation of political liberty, individual enterprise is the foundation of national prosperity.

The times test us. A secure future for our people means responding to the challenge before us with the energy, dedication, and creativity that characterize American business and labor at their best. In this effort, the values of the entrepreneur and the industry of our workforce are genuine assets in the search for change and renewal.

The Commission's mandate reflected the desire of Congress to reduce unemployment by creating ten million jobs through small business. This report addresses the health of the economy as a whole as well as the health of American small business. The Commission was convinced that the problems of small firms are best understood in the context of the national and international economic forces that exert such a powerful influence on American employment and unemployment. By presenting a realistic assessment of where we stand, this report offers the country the opportunity to rethink the potential of entrepreneurs and small business as a force for economic growth.

Sustaining the creativity and growth of small business is crucial to our national vigor. Small firms employ half of our private workforce and produce half of our gross domestic product.

2
Making
America
Work Again

This Commission does not pretend that small business alone can bear the burden of restoring the competitiveness of the United States. We maintain, however, that the initiative and flexibility of small firms can play a vital role in the vigorous, growing economy essential to securing America's place in the world. And we insist that sustaining the creativity and growth of small business is crucial to our national vigor. Small firms employ half of our private workforce and produce half of our gross domestic product. They created nearly two thirds of the new jobs of the last decade and were one of the driving forces behind our advances in technology. Small business represents a powerful resource.

Against a backdrop of relentless change, one domestic imperative stands out: during the next five years, virtually every community in America will have to replace 50 percent of its jobs and businesses. The question is: where will our people find employment?

Although the developments we describe are cause for concern, they are not occasion for alarm. The jobs will be

The Small Business Dimension

According to the Internal Revenue Service, there were over 15 million small firms in 1983, including ten million sole proprietorships, 1.5 million partnerships, and three million corporations. The Small Business Administration (SBA) estimates that about five million of these businesses are actually full-time enterprises with employees.

There is no generally accepted definition of a "small business." Most analysts rely on the number of employees, but there is little agreement on how many. MIT analyst David Birch, the pioneer in small business job generation research, concentrated on firms employing 100 or fewer workers, and attributed most new jobs to a subset of these firms—very small firms employing 20 or fewer people. Others believe 200 is an acceptable limit; the SBA decribes some industries as "dominated" by small business, defined as firms employing 500 or fewer workers.

Small firms provide a remarkable array of products and services. They forge tools and dies, build houses, design and build sophisticated electronic equipment, repair automobiles, manufacture wiring assemblies, mine the earth, program computers, and produce new medical procedures and breakthroughs. The list is nearly endless. They are major employers in mining, manufacturing, transportation, communications, finance, insurance, and real estate. According to SBA data, small firms dominate employment and sales in wholesale and retail trade, agricultural services, forestry, and construction.

Among the contributions of small business to the overall economy:

- **Employment.** Firms with fewer than 100 employees account for 34 percent of all private, non-farm employment; those with 500 or less employ 48 percent of that workforce. Professor David Birch of the Massachusetts Institute of Technology reported six years ago that "60 percent of all new jobs in the U.S. are generated by firms with 20 or fewer employees," an analysis confirmed by studies of local job generation on Long Island, and in Wisconsin, Massachusetts, and California.

- **Gross National Product.** According to the Small Business Administration, small firms produce 38 percent of our GNP and 47 percent of our gross domestic product, that part of the GNP generated by private firms using resources in the United States.
- **Training.** Small firms give two out of three American workers their first jobs, thus making a significant contribution to the education and training of our workforce.
- **Innovation.** In 1986, the Department of Commerce estimated that small companies generated about "50 percent of all major innovations in the past 30 years." A recent study of 635 successful product innovations in the 1970s attributed 40 percent of them to small business and indicated that small firms brought these innovations to the market much faster than larger firms.
- **Opportunity.** Data from the SBA and the National Federation of Independent Business indicate that the number of women-owned businesses has been increasing three times as fast as that of businesses owned by men, and that the number of self-employed blacks and Hispanics has increased substantially in the last ten years.

there—if we prepare ourselves now. The Commission advances a fundamental proposition that has guided us in our work: global competition is the basic economic reality of our time. It has exposed the shortcomings of our educational system. It has laid bare the lack of corporate readiness to compete. It has forced us, in the most recent recession, to rely on small business as the only source of additional jobs in the United States. And it has underscored the necessity to make competitiveness the touchstone of America's economic policy as we make ready to live in a new age and a different world.

The jobs will be there—if we prepare ourselves now.

A Different World . . .

The world of 1987 is far different from that of 1950. A generation ago, a triumphant United States lay secure in its borders, confident of its destiny, and pre-eminent in manufacturing and commerce. We had many advantages others did not: a skilled workforce, productive industries, and a rich and bountiful land. The goodwill of the United States financed the recovery of the free world, and our arms shielded friend and former foe alike as they rebuilt their industrial capacity.

The era of American advantage is over. Modern management and finance, technology, and the worldwide increase in the education and skills of workers have created a global economy. This new international economy has raised standards of living around the world and opened our vast domestic markets to determined competitors. Today, products can be designed in one country, engineered in another, produced in yet a third, and distributed around the globe. Shrewd intelligence, diligently applied, explains why watches once assembled in Switzerland, motorcycles built in England, lenses ground in Germany, and automobiles, steel, and television sets made in America are now manufactured around the Pacific Rim.

. . . And Its Consequences

Lacking a strategic response, we have watched our great manufacturing enterprises falter and our industrial workforce suffer the worst employment shocks in 50 years. We are unable to provide productive work for large numbers of our citizens; we are unwilling to invest adequately in the plant, equipment, education, and technology essential to our international competitiveness; and we borrow more than we are willing to save, preferring to finance consumption at home by piling up debts abroad.

The Commission cannot overstate the seriousness of the economic difficulties now facing the United States. Unchecked, they promise grave consequences for the future.

We borrow more than we are willing to save, preferring to finance consumption at home by piling up debts abroad.

- **A Debtor Nation.** In 1985, for the first time in 75 years, the United States became a debtor to the rest of the world; a year later, the U.S. had become the largest debtor nation in history.
- **Exports.** The American percentage of world exports, measured in constant dollars, shrank by nearly one third between 1960 and 1984. Even in such high-technology industries as aircraft, computers, engines and turbines, scientific instruments, and semiconductors, we have lost world market shares. In 1986, American agricultural trade accounts were in deficit for three months in a row — the first such deficits in 27 years.
- **Productivity.** Since 1970, the growth of American productivity has been cut in half.
- **Growth of the Deficit.** According to the Office of Management and Budget, the national debt doubled between 1980 and 1985. Large annual federal deficits accelerate the growth of the debt. The debt increased at an annual rate of 2.8 percent from 1954 to 1975, at a rate of 11.9 percent from 1975 to 1980, and at a rate of 16.1 percent from 1980 to 1985. Interest on the debt in 1985 totaled nearly $180 billion.
- **Income.** Real wages and salaries, the income on which most families depend, have been falling since 1972. The decline has been virtually indiscriminate: workers in construction, services, finance, insurance, real estate, and manufacturing have all felt the effect. Real personal income per household—including rents, dividends, and interest — shows a similar pattern.

- **Loss of High-Wage Jobs.** We are losing jobs paying $25,000 and more a year in both large and small manufacturing firms and replacing them with jobs in services and retailing paying less than half that amount. Since 1980, America has suffered a net loss of over one million production jobs in manufacturing, paying an average of $13 an hour. At the same time, jobs in services and retail trades, paying between $5 and $7, have increased by 5.5 million.

- **Unemployment.** Unemployment has risen by nearly two percent in each of the last three decades— averaging 4.8 percent in the 1960s, 6.2 percent in the 1970s, and 8.1 percent between 1980 and 1985.

America, meanwhile, has become an import sponge.

- **Automobiles.** By next year, Japan will be the third largest U.S. automaker. By 1990, foreign automobiles, made here and abroad, will account for more than 40 percent of domestic sales.

- **Consumer Electronics.** The market for other consumer goods, particularly in electronics, tells a similar story: we no longer manufacture black and white television sets, and 50 percent of our color televisions and two thirds of our radios come from abroad.

> ***We no longer manufacture black and white television sets. . . . Seventy percent of American manufactured products are subject to foreign competition in the United States.***

- **Manufactured Products.** Seventy percent of American manufactured products are subject to foreign competition in the United States, often with subsidies from their own governments more than four times the assistance available to American exporters.

- **Steel and Textiles.** Since 1960, American steel and textile industries have been badly battered. Imports now account for more than one quarter of the steel used in this country, and since 1970 the U.S. share of world crude steel output has declined from 20 percent to 11.6 percent. The textile trade deficit rose by 16 percent in 1985 and textile employment continued its decline.

These developments help explain why the United States, which between 1891 and 1971 never showed a deficit in its international trade account, has recorded a trade deficit nearly every year since 1971. Trade deficits in the 1980s have grown at an alarming rate. The deficit in 1980 stood at slightly under $30 billion; in 1986, it approached $170 billion.

This array of factors also explains why this generation's concern for the material well-being of its children is well placed. We can already see the signs of these pressures squeezing the American middle class. Too large a proportion of our people live in poverty, and recent economic improvements appear to have benefited those of greatest wealth.

The human consequences of these developments cannot be dismissed. Allowing foreign producers to win domestic markets has helped displace 1.1 million production workers since 1980. Predictions of a brighter outlook for urban America have not borne fruit for the unemployed young men and women of our cities. One witness warned the Commission, "Today we are raising a whole generation that feels it has nothing to lose because it has never experienced even the remote hope of being able to find a job. More than 40 percent of black teenagers are jobless." The 100,000 small farmers who went bankrupt last year find scant comfort in knowing that their farms were swept away because over-extended credit could not cope with fluctuating markets.

Comparable threats to our prosperity and security once evoked a unified and vigorous response from the country. American brains and brawn rose to the challenges of the Industrial Revolution in the nineteenth century and the launching of Sputnik in the twentieth. But we search our recent history in vain for a similar response to help us compete in the dynamic global economy.

The powerful dynamics of the global economy and technological innovation dictate that communities across the country must replace their existing jobs with new ones as the world around them changes.

Despite encouraging demographic trends indicating that the economy will not need to absorb as many young people, creating jobs remains a pressing national need. That need is grounded in a new calculus: the still more powerful dynamics of the global economy and technological innovation dictate that communities across the country must replace their existing jobs with new ones as the world around them changes.

Our economy is not developing apace. Our industry and our government have not responded to the challenge before us by making competitiveness the linchpin of our economic policy. In consequence, we have failed to make the investment in plant, equipment, and machinery necessary to improve our productivity. We have too long ignored the levels of education, training, and skill required in the new workforce. Nor have we capitalized on many unique advantages, including the remarkable ability of the small business community to innovate, to respond to change, and to create wealth and employment.

Threat and Promise

It is easy to lose sight of what is at stake. We are distracted on all sides by strong, determined competitors and by the constant change in the demand for goods and services. We take comfort in material success without understanding that the recent growth of the nation's debt is supported with foreign capital, that too many companies are bowing to the pressure for quarterly profits at the expense of long-term growth, and that, increasingly, two wage-earners are needed to maintain today's family.

We are witnessing nothing less than a fundamental threat to the promise first made in America—that all persons, no matter their station in life, could go as far as the reach of their talents, ambition, and hard work. Although we have not always honored that promise equally for all of our citizens, it has spread the blessings of liberty and prosperity more widely in the United States than in any society known to human history.

The American people need to be clear about the significance of the American promise. It represents far more than a platitude. At the core of the promise is our national affirmation of the dignity of the individual. The pledge that all can create their own destinies holds a powerful appeal to people around the world, and explains why generations of foreigners have sought a better future for themselves and their children on these shores. In offering all citizens the opportunity to pursue their hopes and dreams, the American dream is the source of social mobility in the United States and the foundation of our national economic growth. That promise animates and sustains small business.

Now the legacy is itself imperiled. At stake is not only a fundamental characteristic of the American tradition, but also an element indispensable to the restoration of our economic health and material well-being: the conviction that the individual aspirations of workers, entrepreneurs, and small business owners are a powerful economic force.

It is easy to gloss over one of our hidden strengths. Part of the genius of the American experiment lay in the proposition that political freedom is essential to economic growth. Innovation, the engine of the modern world, prospers only in an environment that encourages new ideas, even at the expense of the old. Our generation's debt to those who 200 years ago created this republic extends beyond gratitude for their foresight in securing democratic government. In fusing liberty and enterprise, they created democratic capitalism, a system of values unparalleled in its potential for creating and broadening wealth.

Now, as we enter our third century, our task is to fulfill the promise of democratic capitalism by encouraging every citizen to participate productively and competitively in the new world economy.

Small Business and the American Future

The Commission believes that the country has at hand the strategic resources needed to realize that promise:

- **Working Spirit.** The spirit of American working men and women who made this nation the most productive enterprise in the world, and who are eager, once again, to make the proud boast "Made in America" the mark of excellence.
- **Business Skills.** The skills of business owners and entrepreneurs in developing new products and services, and their adroitness at identifying and serving new markets.
- **Intellectual Resources.** The great intellectual and technical resources available in our schools, colleges, universities, laboratories, and workshops. They nurture imagination, the soul of technology.
- **Wealth.** A concentration of wealth and financial resources unmatched elsewhere, combined with the most sophisticated capital markets in the world.
- **Technology.** The unrivaled potential of technology, properly applied, to multiply the productivity of labor and capital, reduce costs, improve reliability, and enhance the quality of working life.
- **Confidence.** The confidence of Americans which makes all of us—employer and employee alike—eager to compete as long as the rules of the game are clear, the playing field level, and the referee impartial. That distinctive American trait has emboldened pioneers, immigrants, and entrepreneurs to stake their futures on their dreams.

Urgently needed is the leadership to fashion a national response from these resources to reinforce the bond between private gain and public good. The recommendations in this report present a framework for such a response and, we believe, a compelling agenda for the leaders of American business, government, and public opinion. But the motivating force behind that consensus comes from yet another, more powerful source: the spirit of enterprise itself.

The Spirit of Enterprise

The spirit of enterprise is essential to the dynamic of the American economy. It explains why impoverished students struggle for an education. It fuels the "intrapreneurial" activities of large corporations, intent on generating new ideas and products. It often motivates the nation's foundations and universities in their dedication to defining and solving problems. Properly nurtured, the spirit of enterprise can give life and direction to the many efforts, public and private, required to rebuild our economy.

At its best, small business typifies that spirit. Business incorporations have increased at a phenomenal rate in the United States in the last generation—from less than 100,000 annually in the 1950s to nearly 700,000 in 1986. Although indicative of the direction of change, these numbers are imprecise. No accurate measure of new business formation, including data on self-employment and firms with employees, exists. Incorporation, in fact, may indicate nothing more than the intention to start a firm. Nevertheless, the trend is clear: entrepreneurs have spawned new businesses, indeed whole industries, while mature firms have struggled with changes in the business environment.

Properly nurtured, the spirit of enterprise can give life and direction to the many efforts required to rebuild our economy.

Small firms employing 500 or fewer workers account for nearly 50 percent of private employment and half of our gross domestic product. In the aggregate, those small firms employing 100 people or fewer provide jobs for as many workers as large firms employing 500 or more. According to the President's 1986 report, *The State of Small Business*, employment in industries dominated by small firms grew by more than five percent in 1985. By contrast, employment in industries dominated by large firms grew by less than one percent. The difference continues a pattern of small business job generation stretching back to at least 1976. Studies of job generation over the past ten years show that when job gains and losses for both large and small firms are tallied, small businesses are responsible for more than 60 percent of the new jobs. During the 1981-82 recession, small businesses generated twice the number of new jobs that large businesses lost, in effect accounting for a net gain of one million jobs.

The vitality of American small business lies also in its ability to diversify economic opportunity.

Numerous studies demonstrate the record of invention and innovation of American small businesses. Their contributions are not simply to job generation but also to the training of America's workers, two thirds of whom take their first jobs with small firms.

Other analyses document the fundamental importance of small firms to our national economic strength. In many ways they act as the yeast in our economy, helping to sustain the entire structure. Inter-industry relationships are pervasive and subtle: analyses by the Congressional Research Service indicate that the 1981-82 recession in the housing industry, which is dominated by small businesses, depressed steel and copper orders in the United States as much as did the decline in the automobile industry. The Commission's surveys demonstrate that three quarters of America's great corporations rely on small firms as suppliers, manufacturers, distributors, and customers; four out of ten large firms deal with 1,000 or more small businesses each year. In fact, every automobile worker in manufacturing is supported by four other workers who provide supplies, sales, and services.

This spirit of achievement stands in marked contrast to the flagging economic energy of much of Europe.

The vitality of American small business lies also in its ability to diversify economic opportunity. In the last ten years the number of businesses owned by women has increased three times as fast as that of businesses owned by men. Minority-owned businesses have also grown: the number of self-employed blacks has risen by nearly 50 percent in the last decade, and the number of Hispanic-owned businesses now stands at over 400,000.

It is evidence of the optimism and skill of our business men and women that this spirit of achievement has persevered in even the most difficult economic times. It stands in marked contrast to the flagging economic energy of much of Europe. The accomplishments of small business can no longer be taken for granted as we chart the course of our economic future.

A Simple Prescription

Building on these accomplishments, we can breathe new life into the American economy. A clear and simple prescription can serve as the nation's guide: attend to the conditions that encourage entrepreneurship, business formation, and job creation, or continue to lose ground to others who do.

This precept has served our nation brilliantly in the past. The great industrial and commercial concerns of our nation were built by innovators such as Ford and Bell whose small businesses grew to help shape a new American economy. Our task is to foster the conditions in which their successors can flourish in the new world around us.

Attending to the conditions of entrepreneurship is not a vague national abstraction. Nor are the consequences remote from everyday life. The imperative we espouse touches every town, home, and life. As David Birch of MIT told the Commission, each year we lose nearly ten percent of our jobs and our businesses large and small. Just to break even, he said, every locality in America must replace half of its jobs every five years. Some areas face an even more formidable task: Texas officials told the Commission that simply to stay abreast of change and population growth, they need to create two million jobs within the state by the year 2000.

The best hope of these communities lies in emulating those localities which have already replaced jobs in ailing industries with jobs created by the spirit of enterprise. For example, 10,000 jobs lost in Birmingham, Alabama's steel mills between 1975 and 1985 were replaced by more than 60,000 new jobs in services, many of them in medicine, medical research, and related technologies. Ten years ago the unemployment rate in Massachusetts was the highest in the country as its textile and leather goods industries went under. Today the state's unemployment rate is among the nation's lowest. The state's schools and universities were the base from which entrepreneurs, starting company after company, replaced every one of the 225,000 jobs swept away a decade ago. Most of these new jobs offered outstanding wages, salaries, and working conditions in an effort to attract the highly skilled workers required in new, technologically innovative firms.

Attending to the conditions of business formation promises a growing economy that can employ our people, support our standard of living, and again make American products and services competitive in world markets. Several conditions require priority attention:

Above all, we must bend every effort to give the challenge of international competitiveness pride of place on the nation's economic agenda. . . .

- Above all, we must bend every effort to give the challenge of international competitiveness pride of place on the nation's economic agenda and in our people's thinking. We must understand, not only intellectually but also as a matter of national practice, that our economy is not self-contained, that the marketplace of America is the world, and that our future lies in developing — now — the ability to compete there vigorously.
- The productivity of our workforce and the inventiveness of our scientists and engineers must be multiplied through education, training, and increased support for research, development, and technology transfer.
- The savings of our people must become more disciplined and more oriented toward improving productivity; new private mechanisms to encourage investment in smaller, growing firms must be developed.
- Finally, the public policies, and private organizations and mechanisms of the American economy that support the competitiveness of our small businesses must be strengthened where they exist and created where they do not.

These conditions hold out a vision for a vital America, renewing the promise of the dignity of productive work — if our people are prepared. This vision promises a sound economy, capable of advancing our nation's goals — if our people are productive. A prosperous economy promises new opportunity for our workers, entrepreneurs, and small business owners — if they can but seize it.

Findings and Conclusions

This section presents the findings and conclusions of the Commission in four major areas: (1) preparing our people to compete; (2) encouraging greater savings and investing them productively; (3) expanding export opportunities, including those for small businesses; and (4) minimizing the impediments to the growth of small firms.

Much of what we have to report causes us concern, not only because of the impact of these factors on businesses large and small, but also because of the complexity of the environment in which these difficulties are embedded. Demographics, tax policy, and the productivity of workers abroad affect our workforce nearly as much as the foresight of our leaders in government, business, and industry. Although these broader issues frame our thinking, our task is not so much to analyze causes as to address consequences. Our findings and conclusions, therefore, are the basis for recommendations on what needs to be done, not a brief for assigning blame.

Our People Unprepared

Of particular concern to the Commission are signs that our people are not armed with the knowledge they need to deal with the changes around them. Two weaknesses stand out. First, the quality of our workforce—blue- and white-collar alike—must be improved. We must act on our understanding that education bears directly on our economic health and well-being. Second, that educational effort must be more firmly grounded in a clear perception of the changed conditions of enterprise in the modern world and of the dynamics of the economy that supports us.

We must act on our understanding that education bears directly on our economic health and well-being.

Education and the World of Work

The speed of change in today's business world demands unprecedented levels of skill, commitment, and flexibility on the part of our workers and managers. Our educational institutions are not, in the Commission's view, preparing our young people for the lifetime of change that lies before them.

Too many young people, even the well educated and well trained, are unable to bring the skills they have acquired to the tasks before them in productive and competent ways. Nor has our workforce acquired the ability to reconfigure those skills to meet new challenges and solve new problems. Even our schools of business have concentrated on developing executives to manage people, wealth, and resources, largely ignoring the need to develop the entrepreneurial talent to create wealth and resources.

Too often a weak educational program in our schools and colleges is followed by an inadequate system for delivering continuing education and retraining to the workforce. Many students appear content to do the minimum necessary to obtain their secondary certificates or college diplomas, hoping to slide by in their adult years with what they learned in the first 20. And, while other countries consciously work to train and retrain large portions of their workforces each year, we seem content with uneven efforts to provide training and retraining for only one half of one percent of ours.

There is widespread agreement that serious attention must be paid to upgrading the skills of the American workforce:

- **Functional Illiteracy.** Millions of Americans are, for all intents and purposes, illiterate, unable to comprehend the simplest written instructions. Although precise figures on the number of illiterate Americans are a matter of debate, the economic impact of widespread illiteracy is beyond dispute. Figures from the 1980 Census indicate that about 75 percent of the unemployed are "functionally illiterate," and the Business Council for Effective Literacy estimates that welfare and unemployment support related to illiteracy costs up to $6 billion annually.
- **Skills of Secondary School Graduates.** The reports of many recent commissions and other prestigious bodies

concerned with education have documented the declining skill levels of the average high school graduate. Of particular concern to this Commission are the findings of the National Assessment of Educational Progress (NAEP) indicating that "higher order" skills such as reasoning, problem solving, and writing are substantially below the standards required for success in the modern world. For example, in a 1986 NAEP examination of writing skills, only 25 percent of 11th graders were judged "adequate," raising serious questions about their ability to succeed in school, business, the professions, or government.

- **No Coherent Training Policy.** Vocational schools, community colleges, public service employment, and youth training activities strive to train and retrain the workforce, but there is no sustained, coherent public policy toward training to support them. Since 1962, the federal government has adopted and abandoned 14 different training strategies. Greater stability in these efforts would surely produce better results.
- **Engineering Shortage.** Half of the students in American graduate schools of engineering are from foreign countries. Our supply of highly skilled engineers, and the teachers who will one day train them, is seriously threatened. Not only are we failing to educate the new generation that will develop and implement our own manufacturing technologies, we are exporting the trained talent that strengthens our competitors in world markets.

By the year 2000, America may have a shortage of as many as 15 million scientists, engineers, skilled mechanics and semi-skilled workers.

We can do better. Indeed, we have no choice: analyses by Nobel Laureate Wassily Leontief, professor of economics at New York University, indicate that the rate of technological change in American work life portends a deepening crisis in the skill levels of our workforce. By the year 2000, America may have a shortage of as many as 15 million scientists, engineers, skilled mechanics such as machinists, and semi-skilled workers including assemblers and welders. A similar number of managers, sales personnel, and clerical help will face a glutted job market and unemployment.

Understanding the Changed Conditions of Enterprise

Several analysts and surveys point to a widespread lack of understanding of our economic difficulties and of the workings of our economy.

> ***Even as foreign competition stalks domestic markets, only a fraction of our businesses export their products.***

- **New Competitive Environment.** There are several indicators that neither our businesses nor our leadership are reacting appropriately to new international conditions. Even as foreign competition stalks domestic markets, only a fraction of our businesses export their products. The rapidly changing economy poses a fundamental challenge to the traditional view of work and career: all of us can expect multiple job and career changes during our working lives. Our diplomatic and commercial interests are tongue-tied by the inability of Americans to speak the languages of other lands or to understand their cultures.
- **No Understanding of Entrepreneurship.** University of Michigan researcher John Jackson testified before the Commission that the public has little or no understanding of the job-creating role of small business in the United States, or of the contributions of entrepreneurs.
- **Lack of Knowledge of Economics.** A disquieting number of American high school students, according to the Joint Council on Economic Education, do not understand how the American economy works. Surveys indicate that education in economics is not required for high school graduation in most states and school districts. In consequence, students are unfamiliar with the role of business, government, and labor in the economy; nor do they grasp such basics as supply and demand, the importance of trade, and the relationship between productivity and wages.
- **Educators Equally Uninformed.** Educators are equally uninformed. Far from understanding capitalism as a system for creating wealth, many of them think first of its excesses. Few American schoolteachers have completed even a single economics course in college, and only eight percent of American adults were taught economics in school. Nearly seven times as many adults report that their understanding of economic issues comes mainly from commercial television.

Surely it is not too much to ask that our schools provide graduates with the knowledge of the changing conditions of the world in which they must earn a living. Despite isolated efforts, most students appear to leave school underinformed—even misinformed—about economic matters, including the role of business in American life.

Savings and Investment Inadequate

At the heart of any nation's efforts to improve its productivity must be a commitment to invest in plant, equipment, and new technology. Yet, compared to the efforts of our economic competitors, American capital formation is inadequate. We have encouraged consumption at the expense of savings and investment, much of the available financing is diverted unproductively, and our financial markets are directed toward short-term profits at the expense of long-term productivity improvements. Most surprising of all in the country with the most sophisticated capital markets in the world, we found that few mechanisms exist to help the average American invest in small firms—the firms that have created most of the new jobs in the last 20 years.

> ***Despite isolated efforts, most students appear to leave school underinformed—even misinformed—about economic matters.***

- **Savings.** The American savings rate ranks last among industrialized nations. Other nations, including West Germany, Canada, and France, save and invest far more than we; Japan saves nearly four times as much. The growth of the United States federal deficit in the last six years has absorbed about 50 percent of the private sector's normal savings.
- **Cost of Capital.** By international standards, the cost of capital to American business is extremely expensive. Recent analyses indicate that capital is twice as expensive in America as in Japan, a competitive burden to American business at least equal to the cost of American wages and salaries.

- **Use of Capital.** Last year was the third consecutive year in which corporations raised as much debt to finance mergers or protect themselves from raiders as they raised to invest in new equipment, facilities, and financial assets.
- **The Narrow Base of Capitalism.** Very few Americans purchase stock. Although millions own stock indirectly through Individual Retirement Accounts, pensions, insurance, and mutual funds, only seven percent of our people own stock directly.
- **Capital Unavailable to Small Business.** Witness after witness told the Commission about the lack of long-term capital for small business. They pointed to legal restrictions prohibiting major institutional investors, including the managers of pension funds and IRAs, from investing in small firms. They also emphasized that capital for minority enterprise was a particular difficulty.

The American savings rate ranks last among industrialized nations.

- **Aging Equipment.** Seventy percent of the manufacturing equipment in the United States is ten years old or older, compared with only 40 percent in Japan.
- **Consumer Debt.** Consumer debt in America, excluding mortgages, exceeds $575 billion — triple the level of a decade ago — a phenomenon encouraged until only recently by policies that both taxed interest on savings and permitted deductions of interest on loans.

Analysts reviewing these data have come to sobering conclusions. Professor Bruce Scott of the Harvard Business School told the Commission that the United States has been losing its capacity to compete in the world economy and that America "leads the world in consumption, is last among the industrialized nations in savings, and is well on its way to becoming the biggest debtor ever."

Economist and business owner George Hatsopoulos provided a similarly grave warning: "A dramatic and frightening change is underway, which must be addressed before our bubble bursts. . . . If our competitors invest three times as much per worker as we do, we will lose jobs, our productivity will decline, and they will take markets away from us."

Problems of the Small Firm

The inadequate capital environment in the United States creates difficulties for all businesses, but particularly for the small firm.

- **Venture capital.** The Joint Economic Committee of Congress reports that many worthwhile proposals cannot be financed. All across America, small business men and women report that venture capital is largely unavailable for new firms. According to the Joint Economic Committee, "Only the cream of the crop of entrepreneurial investments receive funding from the venture capital community."
- **Long-Term Financing Difficult.** Established small firms can obtain only short-term financing from local banks—often at high interest rates. Most small firms report a total lack of long-term funds, i.e., money for 60 months or longer.
- **Bias Against Small Business Investment.** Congressional surveys report a "bias" against small business investment on the part of the financial community, stemming in part from a misunderstanding of small business, the difficulties of administering a loan portfolio with many small loans, the prohibitions against financial institutions holding an equity position in the companies of their borrowers, and the lack of a developed secondary market to recycle small loans.
- **Raising Equity.** Securities regulations, though recently simplified for small business, are still cumbersome, and the process of offering stock is so expensive for small issues that many small firms find it easier to raise equity on foreign exchanges.
- **Impact on Minorities.** These problems are nearly insurmountable in minority communities, most of which lack the resources the small business owner needs, especially the pool of capital that family and friends can provide.

Urgently needed . . . are new mechanisms and financial instruments to increase the volume of capital investment in small firms.

It is impossible to avoid the conclusion that the capital needs of the small business owner have been largely ignored by the institutions that dominate banking and finance, as well as by those who make policy governing those institutions. This situation was easier to understand when the country could rely on great corporations for its economic growth, and when banking institutions were naturally attracted to the efficiencies of large financial transactions. But self-sustaining

Tax Reform Act of 1986

The Tax Reform Act of 1986 represents a major restructuring of the federal income tax system. The legislation reduces the top tax rate for most individuals to 28 percent, and reduces the top corporate tax rate to 34 percent. It is estimated that the Act will reduce the tax burden on individuals by approximately $120 billion over the next five years, while corporate taxes increase by a similar amount.

Among the new law's major provisions relating to business are these:

- Reduction of the top corporate income tax rate from 46 percent to 34 percent.
- Elimination of the provisions for long-term capital gains for both individuals and corporations. The maximum individual capital gains rate will rise from 20 percent to 28 percent for most taxpayers. The corporate capital gains rate will rise from 28 percent to 34 percent.
- Elimination of the investment tax credit (ITC), now worth up to ten percent of the cost of machinery and equipment, retroactive to January 1, 1986.
- New, longer depreciation schedules for writing off investment in plant, machinery, and equipment, meaning smaller deductions each year.
- Extension of the Research and Development tax credit through 1988 with a reduction in the value of the credit from 25 to 20 percent.

prosperity is no longer possible if inventors, entrepreneurs, and even mature small firms are left to struggle to find their financing.

Urgently needed, in the Commission's view, are new mechanisms and financial instruments to increase the volume of capital investment in small firms. When the country recognized the importance of expanding housing and student loans, financial institutions and the federal government together created the necessary financial vehicles. Those precedents can serve as models to help provide small firms with investment capital while covering investors' risks, providing a reasonable rate of return, and offering the liquidity that small investors require.

The Reluctant Exporter

Although the Department of Commerce estimates that each $1 billion in expanded exports supports nearly 25,000 domestic jobs, we do little to encourage small firms to export.

Improving this situation requires our society to take up a formidable agenda:

- **Few Exporters.** Only ten percent of American firms export, and just 250 companies account for nearly 80 percent of the dollar volume of American exports. An estimated 30,000 small firms provide exportable goods and services; in fact, these firms export nothing at all because for many of them foreign markets are the invisible option. Efforts by national and state government to identify, reach, and serve these firms are, according to testimony before the Commission, "notably deficient."

Only ten percent of American firms export. Just 250 companies account for nearly 80 percent of the dollar volume of American exports.

- **Export Decline.** Between 1980 and 1982, in the depths of the recent recession, small business experienced an absolute decline of 15 percent in real exports, twice the decline of all U.S. exports. We might anticipate that further erosion of American competitiveness will strike these firms first.
- **Lack of Government Assistance.** Only one percent of the Small Business Administration's loans were used for exporting between 1983 and 1985, and no export loans were made in 1986. Eximbank, which provides federal

support for the sale of American products abroad, has not used the full amount of loans and guarantees for small firms authorized by Congress.

- **Too Many Agencies.** The bewildering array of official agencies is a problem in its own right. The U.S. Foreign and Commercial Service in the Department of Commerce provides useful information on foreign markets but cannot provide export financing. Those agencies with the financing available appear unwilling to provide it to small firms. The recent enactment of legislation authorizing Foreign Sales Corporations (FSCs) and Export Trading Companies coincided with fluctuations in the value of the dollar and growing interest in tax reform, leaving both mechanisms in limbo.

At the same time, foreign business owners enjoy official support that "turns me green with envy," one small exporter told the Commission. Sponsorship of trade delegations abroad, assistance with shipping and letters of credit, joint ventures to spread risk, certain tax preferences, as well as financing to cover pre-export costs and collecting receivables are all perfectly acceptable under the General Agreement on Tariffs and Trade (GATT). For a variety of reasons, such mechanisms are largely unavailable to the American business owner.

Obstacle Course for Growth and Competitiveness

The most fertile environment for business growth and vitality encourages entrepreneurial risk and minimizes barriers to expansion. But the environment in which businesses operate today falls short of that standard. Businesses are, in fact, hampered by two sets of conditions—one self-generated and the other external. Both choke growth. On the one hand, our economic health depends on business policies and procedures that encourage growth and risk-taking. Instead, within business, we find outdated and internally contradictory perspectives that stifle initiative and reward playing it safe.

Within business . . . outdated and internally contradictory perspectives stifle initiative and reward playing it safe.

Legislation, regulation, and litigation, on the other hand, add to the cost of American goods and services. These difficulties make business decision-making more complex, seriously hindering innovation and expansion. The Commission understands that such issues as environmental and occupational safety, consumer protection, and the integrity of financial markets are important national goals. Nevertheless, we believe it is possible to achieve them without a maze of agencies and red tape.

Ironically, the things that make profits possible in the long run are being sacrificed to the cosmetics of a short-term outlook.

These two sets of conditions have combined to create a climate which itself threatens the dynamic nature of American business and impedes its ability to compete:

- **Political Difficulties.** Government seems unable to deal effectively with the major economic issues of our time: the budget and trade deficits, the value of the dollar, inflation, unemployment, the cost of capital, and regulation. The political process itself often has difficulty discerning where the public interest lies in the welter of conflicting claims and counterclaims.
- **Myopic Management.** The necessity to replace plant and equipment, to invest in a productive workforce, and to produce quality goods at competitive prices has too often been ignored by management. Ironically, the things that make profits possible in the long run are being sacrificed to the cosmetics of a short-term outlook.
- **Difficult Labor-Management Relations.** Although the leaders of many unions and industries have responded to the imperative to improve labor-management relations, more action is needed. Both labor and management must cooperate to produce a healthy, competitive economy.
- **Clogged Courts.** The law is changing so rapidly that most business owners understand neither their obligations nor their rights. It takes years to resolve even the simplest matters in our courts; judgments in ordinary tort cases are less and less based on fault and more and more on the depth of the defendant's pockets.
- **Liability Insurance.** The insurance crisis has reached alarming proportions. Premiums and judgments have skyrocketed. Different states apply different criteria in tort

cases. Important public purposes ranging from job creation to environmental control are threatened as business owners hesitate to take advantage of markets in which litigation is to be expected.

- **Limited Information.** Information in the modern age is indispensable. But the official data available to the business owner are seriously flawed. The government collects mountains of information but much of it is not readily accessible; most is not timely; and useful information about foreign markets is lacking. Ignoring the rapidity of change, the government continues to collect data describing a vanishing industrial past. For example, we can compute the number of workers sewing buttons on shirts, but we cannot pinpoint the number of computer salesmen.
- **Banking Turmoil.** American financial institutions can now engage in a wide variety of activities abroad that are prohibited in the United States—including underwriting corporate securities. The recent deregulation of London's financial markets promises to accelerate this development.

In sum, the business landscape is scattered with hurdles to initiative, imagination, and innovation. These obstacles stifle growth and undoubtedly add to the cost of American goods and services on world markets. The success of small firms in recent years demonstrates their ability to cope with these difficulties. Nonetheless, evidence before the Commission clearly showed that too much time and energy is misspent dealing with "the system" instead of with business.

Recommendations

In light of the need for action, the Commission has agreed on five recommendations. The difficulties we have defined, though severe, are not insurmountable. The major task lies in forging the national will to respond to the competitive challenge before us.

The recommendations of the Commission serve three broad purposes. First, they outline institutional mechanisms to focus sustained attention on the problems we have discussed. In this regard they are but the first steps in a continuing and difficult process. Second, they suggest some immediate actions to improve our economic performance and particularly, to utilize an asset that has, until now, been largely ignored—small business. Finally, the Commission hopes to define some common ground on which the leaders of industry, small business, government, education, and labor can agree.

The recommendations serve as suggestions for what we need to do, not as rigid guidelines for how to do it. As such, they represent a starting point for productive debate.

Recommendation A

Mobilize Our People

We recommend a major effort, engaging the attention of public and private leaders nationwide, to alert Americans to the realities of the new world economy, to improve public understanding of our economy and the role of enterprise in it, and to emphasize Americans' opportunities for full employment through creative participation in the nation's economic life as entrepreneurs, business owners, and employees.

Implementing Recommendations

1. Public Leadership. Elected officials should take the lead in developing, sponsoring, and articulating the message about the basic elements and dynamics of the new world economy to our people. Specifically, all governors should lead an examination of the effects of international competition within their states, including attention to its impact on jobs and on small firms. Local officials should foster a fertile climate for small business and employment growth, encouraging new firms to start and existing firms to expand. Federal officials should insist that issues of employment and competitiveness remain high on the national agenda and should marshal the political will and confidence of our people to respond to the tasks before us.

2. Private Sector Leadership. Unions, corporate executives, business owners, and their trade associations should increase their efforts to inform their employees and members of the issues described in this report. We urge corporate and union leaders together to develop educational initiatives to inform the workforce of company plans and prospects for the future and to stress each employee's personal stake in the global economy.

3. Public Understanding. In light of the extraordinary importance of these matters, the President should deliver an annual message to Congress on improving the nation's competitive position and expanding employment opportunities for the American people. Communications leaders in newspapers, magazines, television, and radio should provide more and better analyses of issues relating to the health of the American economy.

4. Education. Each state board of education should act to insure that today's students are prepared to function in tomorrow's world. The study of foreign languages and cultures is essential, as is a solid preparation in modern history, current affairs, and world geography. Social science and economics are also important if our young people are to understand the values, dimensions, and benefits of our economic system. In this effort, particular attention should be paid to the quality of teaching since so few schoolteachers themselves understand the dynamics of our economic system. All prospective teachers should study economics.

5. Education for Opportunity. Those who dream of creating a business need the skills to run one. Every state should review the educational offerings of its schools—in particular, its vocational programs in secondary schools and community colleges—to make available training in business creation, including business and financial planning, cash flow management, employee development, and managing and consolidating growth. Efforts should be made to involve small business owners in developing these curricula as well as in teaching.

Recommendation B

Prepare Our Workforce

We recommend national efforts to: (1) provide workers and managers with the skills required to compete in and adapt to the new business environment; and (2) develop the flexibility needed to begin new roles, even new careers, in a changing economy.

Implementing Recommendations Regarding Skills

1. Early Learning. Today's infants will be the entry-level employees of the 21st century. Educational research demonstrates convincingly that uncorrected early learning deficiencies are compounded with the passage of time. We believe that to help assure a productive and competitive workforce, every community should provide stimulating preschool learning environments, available on a voluntary basis, and more rigorous elementary school education to prepare students for high school.

2. Educational Standards. Implementation of the recommendations for more rigorous school standards for students and teachers of the National Commission on Excellence in Education and of the Carnegie Forum on

Education and the Economy is essential and long overdue. Following through on these reforms will lead to American workers, managers, and teachers who are more skilled, more adaptable, more conscientious, and better prepared for the world of work. We urge business leaders to set aside time to work with local schools and colleges in support of these efforts. Many tasks need attention: guest lecturing, volunteering for education task forces, hosting visiting student groups, and other activities that create business-education partnerships.

3. Mathematics and Science. The pressing need for improved mathematics and science instruction to upgrade the technical skill of our workforce must be addressed by efforts such as: (a) stronger requirements for course completion for high school and college graduation; (b) salary supplements to attract more able teachers of mathematics and science to our secondary schools; (c) grants and forgivable loans to encourage undergraduates to pursue careers in science, mathematics, engineering, and teaching; and (d) magnet schools for particularly talented students in math and science.

4. Colleges and Universities. Public and private colleges and universities, including community colleges, have an extraordinary array of resources that can assist local, state, and regional economic development. We recommend that each educational institution work with local public, business, and labor leaders to decide which of the following resources it can best provide:

- research and analysis,
- training programs,
- technology transfer efforts,
- entrepreneurial institutes, or
- centers of excellence in areas of outstanding faculty strength.

Implementing Recommendations to Encourage Flexibility

1. Training and Retraining. Private and public efforts to train, retrain, and enhance the skills of employees need to be expanded. We recommend: (a) business support for educational leave and tuition reimbursement for employees' educational expenses; (b) amending existing public job-training programs to encourage local public agencies to place participants in internships with small business; (c) carefully designed and managed employment opportunities in the public sector, accompanied by mandatory education and training, that will provide job experience for poorly skilled entry-level workers and encourage regular work habits.

> ***We have an obligation to create jobs that offer a future of self-development—jobs that are not merely life sentences to drudgery.***
>
> John Sloan
> National Federation of
> Independent Business

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2. Employers and Training. Because U.S. employees frequently change jobs, employers are less inclined to sponsor training and retraining. Federal and state governments should encourage business investment in employee development through special tax or other incentives.

3. Individuals and Training. Existing individual exemptions for employer-financed education and training, scheduled to expire in 1987, should be maintained and made permanent. Many economists and business leaders have suggested that businesses cooperate with their employees to establish individual training accounts, similar to Individual Retirement Accounts, as a mechanism for upgrading skills and developing new ones. We believe this idea, including the possibility of tax deferrals on contributions and on the interest they earn until used, is worthy of serious exploration and experimentation.

4. Portable Pensions. In the new economy, where career change is a constant, the pension structure must be simplified to enable employees to plan their retirement security. The first step is to accept the principle of a pension that travels from job to job and employer to employer. Varying structures for implementing this principle have been proposed; all have merit. It is time to act on the principle.

Recommendation C

Invest In Our Future

We recommend doubling business investment in plant, equipment, and technology in the next five years. Special attention should be given to providing small firms with new streams of capital and to promoting "people's capitalism" to enable more citizens to take a stake in the success of American business as equity holders. Critical to reaching these goals are instruments and mechanisms to provide liquidity, safety, and a reasonable return on investment to investors.

The incentives proposed below include encouraging greater national savings; improving investment credits; expanding stock ownership, especially equity participation in small business mutual funds; encouraging research, development, and technology transfer; increasing state efforts to assist small business; and encouraging business formation in distressed areas. These proposals offer no special advantages for small business. They are designed to erase the obstacles faced by small business in our capital markets—obstacles that have already been removed for other larger users of capital.

Implementing Recommendations

1. Savings. Net national savings—the sum of private and public savings, less public deficits—must be increased by encouraging greater personal saving and by reducing the federal deficit. We believe that national policy should encourage people to save and that reducing the taxation on savings is sound public policy. We consider it essential that federal revenues and expenditures be brought into balance at approximately 20 percent of the gross national product.

2. Reestablish the Investment Tax Credit. We recommend reestablishing the Investment Tax Credit. We believe the credit should be focused to make it more useful to small business and that the potential for abuse of the credit can be minimized if it is directed at machinery and equipment essential to improving productivity.

3. Holding a Stake in American Prosperity. We recommend linking the success of American business to the direct financial interests of the American worker by democratizing financial markets and permitting far more citizens of moderate means to acquire an equity stake in business. Specifically, we urge:

- Structuring benefit programs that encourage employee participation in investment funds. Numerous well-managed and successful thrift plans already exist to serve as models.
- Expanding opportunities for profit sharing and employee stock ownership for American workers. The systems required include routine consideration of such opportunities during company reviews of benefit programs, financial mechanisms to help employees gather the capital they need on terms they can meet, and disinterested, expert assistance in analyzing the merits of employee ownership.

4. Small Business Mutual Funds. We recommend the establishment of small business mutual funds in the private sector, to direct substantial capital investment into job-creating small businesses. We strongly recommend that new mechanisms be created so that major sources of savings and capital—pension funds, IRAs, insurance companies, and trusts—can prudently invest substantial assets in small businesses. The necessary mechanisms include: protecting against loss through self-insuring set-asides; providing an attractive rate of return including participation in equity growth; and offering investor liquidity.

> ***In the next five years, robots may replace over seven million manufacturing jobs.***
>
> **Lawrence Crockett**
> **Institute of Science and Technology**
> **University of Michigan**

5. Public/Private Partnerships for Small Business Investment. Federal, state, and local governments should join in partnership with the private sector to significantly increase the volume of long-term, fixed-rate, small business loans. Specifically, we recommend:

- Improving the existing small secondary market for small business loans to make it comparable to existing markets for student and housing loans. A more vigorous secondary market can be created if the federal government: (1) encourages financial guarantors, including insurance companies and bank holding companies, to provide loan insurance to small firms; and (2) reinsures these insured loans against catastrophic loss.
- A federal-state guarantee program, similar to federal-state housing coinsurance, to encourage states to coinsure federal loans, thus permitting the federal government to

reduce its exposure to 50 to 70 percent of each loan.

- A primary loan guarantee program combined with greater lender discretion and accountability, directed at newer firms and women- and minority-owned businesses. We believe the federal guarantee for these loans might be as high as 90 percent.

> ***The truth is, as far as any small business owner is concerned, the capital markets in this country just don't exist.***
>
> **Sara Loveland**
> **National Development Council**
> **New York, New York**

6. Encourage Long-Term Capital Investment. The tax structure should encourage long-term private investment for growth and reward the assumption of risk. Several analysts, for example, have suggested indexing capital gains taxation by the number of years the investment is held as well as granting more favorable treatment for long-term investments in small firms. At a minimum we consider the following essential:

- Long-term investment in productive assets should be encouraged by taxing gains from such assets held over a five-year period at a rate lower than the rate for ordinary income, with consideration given to a yet more favorable rate for investments in new or smaller companies.
- Investment in "illiquid" new and small companies should be encouraged by reducing arbitrary barriers to equity investment. For example:

—Subchapter S of the Internal Revenue Code is a desirable form of incorporation for many small firms but it is restricted to businesses with not more than 35 individual shareholders. We believe the permissible number of shareholders should be increased to 100 and that venture capital funds should be permitted to invest in these corporations.

—The Securities and Exchange Commission in 1982 adopted "Regulation D" governing small offerings of private securities. More onerous state requirements should conform to the SEC requirements.

—Pension fund "prudent investor" rules are essential. We believe they should be applied to a pension's entire portfolio, and that federal "plan assets" requirements should encourage pensions to invest between one and three percent of their assets in new and growing companies and in venture funds.

—An Inflation Index should be developed so that capital assets held for the long term can be indexed in order to tax investors on the basis of real economic gain, not on the basis of inflationary gains.

7. Research, Development, and Technology Transfer. We recommend:

- Increasing public and private support of university-based research, development, and graduate education.
- Increasing the highly successful Small Business Innovation and Research Program (SBIR) to three percent of existing government research and development expenditures.
- Creating, in every state, support systems for technology transfer that encourage partnerships between the academic and small business communities. Such partnerships can help commercialize university-based research and development and serve as a forum to introduce academic engineers and scientists to their counterparts in small technology-based firms.

> ***Tiny Asian sewing shops have devastated American garment industry giants. . . .***
>
> **Erwin von Allmen**
> **W.C. Smith Inc.**
> **Philadelphia, Pennsylvania**

8. Partnerships for Job Creation. States should provide incentives for insurance companies, banks, bank holding companies, savings and loans, pension funds, and foundations to create private, state-chartered partnerships to focus on job creation through investment in "targets of opportunity." Targets could include biotechnology, robotics, CAD-CAM (computer-assisted design and manufacturing), small manufacturing, community-based housing and entrepreneurship, and programs for training displaced workers, minorities, women, and other entrepreneurs new to the mainstream. Job creation should be a fundamental goal.

9. Incentives for Independence. Government efforts to provide public assistance and unemployment compensation must be complemented with efforts to encourage self-employment and entry into the labor market. Experiments should coordinate a variety of services required to obtain and keep a job, including education and training, child care, transportation, nursing care for home-bound relatives, and other aids to employment and self-employment. Such experiments can succeed, however, only if participants continue to receive benefits at least during the initial stages of the transition.

10. Experimentation. State and private leadership is needed to establish small business incubators, enterprise zones, community development corporations, and other experiments to encourage business creation and expansion in distressed urban and rural areas. Federal efforts in economic development should support these innovations and encourage local initiatives that respond to local problems.

Recommendation D

Restore the "Yankee Trader" Tradition

We recommend continuing the policy of the United States that supports the fair trade of goods and services among countries, combined with an aggressive, visible, high-priority program to restore a vigorous, exporting industrial base that will include large numbers of smaller firms.

Implementing Recommendations

1. Expanding GATT. The United States should continue its emphasis on including services, intellectual property rights, and agricultural products in the scope of the General Agreement on Tariffs and Trade (GATT).

- The U.S. Trade Representative, in the current negotiations, should seek GATT recognition of the economic burden the United States bears in assuming a major share of the defense costs of most of our trading partners in Europe and the Pacific Basin.
- The U.S. Trade Representative, in negotiating GATT terms, should insist that all signatory countries comply with the spirit and intent of the Agreement. Penalties or countervailing procedures should be invoked where violations are found and documented.

2. Import Quotas. Import quotas and voluntary restraints obviously impede trade. Those now on the books should be periodically reviewed. If the quotas or restraints cannot be justified, they should be removed. If found appropriate, quotas and restraints should be enforced and maintained.

3. Expanding Exporting Base. Specific incentives should be enacted to attract new companies into the exporting industrial base and to encourage those already exporting to expand. For example:

- Improve and simplify the Foreign Sales Corporation provision to make it more useful to smaller firms.
- Require Eximbank to market its existing small business export financing programs more aggressively. State governments should strengthen their export financing programs to expand the availability of funds.
- Create a Small Business Exporting Incentive program similar in structure to the existing Small Business Innovation and Research program.
- Seek alternative methods under GATT to allow U.S. exporting companies specific cost reductions through tax incentives to match the tax incentives available to businesses in other countries.

4. Serving Small Business. Improve the education of small businesses in exporting by:

- Working aggressively with states and small business groups to disseminate information concerning programs of the International Trade Administration (ITA) already available to small firms.
- Reorienting ITA export promotion programs to focus specifically on small business participation. Measures of effectiveness tied to expansion of the exporting industrial base, rather than the short-term dollar value of exports, should be applied.

> ***No business today—large or small—can afford not to think of the impact of this globalization trend.***
>
> **The Honorable Clarence Brown**
> **Deputy Secretary**
> **U.S. Department of Commerce**

- Improving implementation of the Export Trading Companies Act by actively assisting the formation of ETCs. We believe that, if the anticipated benefits of authoring

ETCs are ever to be realized, a serious commitment to large ETCs is in order. Other mercantile nations combine the resources of government, business, and financial centers to encourage exports and we can do no less.

5. Marketing Data. Improve the flow of marketing data by:

- Developing an International Commerce Business Daily to provide timely marketing leads to small firms nationwide. The publication should be tied into the U.S. and Foreign Commercial Service computer system.
- Creating incentives for multinational corporations to use U.S. small businesses as subcontractors in overseas projects.
- Providing incentives for large companies to assist small U.S. companies abroad by use of facilities and market leads.
- Establishing a public-private partnership to provide market information and analysis to the business community, similar to that provided by the Japanese External Trade Organization (JETRO).

We should not subsidize failure; the bulk of the risk should continue to be on the entrepreneur's shoulders.

Patrick A. Thompson
Trans-Matic
Holland, Michigan

6. State Leadership. Leadership on the part of state governments to encourage exporting is essential to take advantage of the considerable economic power of individual states and the closeness of state governments to small firms. We believe every state should set a goal of increasing small business exports by ten percent annually. Working with Department of Commerce regional offices, each state should:

- Analyze its own trade flows with other nations to identify both imports of great demand within its own borders and its own products that are in demand overseas.
- Establish promising exchange relationships with representative nations around the globe—one, for example, in the Pacific, one in Latin America, one in Africa, and one in Europe—to help its small firms gain experience in trading, as well as learn the language and customs of different parts of the world.
- Sponsor small business exporting initiatives such as

financing mechanisms, trade delegations abroad, state-sponsored Foreign Sales Corporations, and trade missions.

7. A Conference of Summit Nations on Small Business. The economic summit nations should build on their 1986 statement that technological innovation and small business expansion are the keys to non-inflationary economic growth by organizing an economic summit conference on small business and trade. We recommend that the President of the United States and the leaders of the other summit nations convene such a conference between 1990 and 1992 that would:

- put small business owners around the world in touch with each other;
- encourage American business owners to learn how others organize themselves for exporting;
- permit others to learn how American small business succeeds in our environment;
- provide small business participants the opportunity to understand the development of policy for international trade; and
- open the possibility of greater consideration of small business in GATT.

We believe the 1986 White House Conference on Small Business could serve as a model for such an international conference.

Recommendation E

Clear the Decks

We recommend that the institutions responsible for economic growth in the United States—government, business, labor—reorganize their structures and processes to reflect the new realities of global competition, the imperative to restore American competitiveness, and the powerful role of small business in America in meeting these challenges.

Implementing Recommendations

1. The Test of National Policy. In developing national economic policy for the coming decades, priority should be given to two considerations:

- Does this policy contribute to America's ability to compete in the world?
- Does it support job creation, business expansion, and small business growth?

These tests set a demanding standard. The Commission is quick to acknowledge that even policies which fail both tests might make good public policy; nevertheless, putting the questions should make us aware of the consequences of our decisions.

2. Organizing for Global Competition. In both the executive branch and Congress, trade-related functions must be coordinated, and responsibility for improving our competitive position assigned. With respect to the executive branch, cooperation is essential among the Department of Commerce, the Small Business Administration, the Departments of Treasury, State, Agriculture, and Defense, and the Office of the United States Trade Representative. The President and Congress should either act to create a Department of Trade to unify our trade policy and activity, or the President should devise other means to eliminate bureaucratic overlap, clarify lines of authority, and correct indecisiveness in our trade policy.

The dispersion of responsibility for matters related to international competitiveness among the committees and subcommittees of Congress is also a difficulty. We urge the committees of Congress with jurisdiction over issues related to international competitiveness to exercise keener oversight of these issues in order to keep these matters before the public.

3. Public and Private Cooperation. We applaud the significant private leadership demonstrated in the work of such groups as the Committee for Economic Development, the Business–Higher Education Forum, and the newly-formed Council on Competitiveness. We believe the work of such groups can be complemented effectively by a public–private partnership in the form of a standing body to analyze domestic economic growth and American competitiveness. Congressionally chartered, but privately supported, the Council should include state and local public officials, corporate leaders, financiers, small business owners, educators, and representatives of American labor. Its charge should be to assess American competitiveness, including the impact of government regulations, the health of small business, the adequacy of government data, and the effect of legislation and judicial decisions on the economy. Of special concern in the immediate future is assessing the consequences for economic growth of the tax legislation of 1986.

4. The Budget Process. The monumental accomplishment of the 93rd Congress in creating a Congressional budget process can be improved by the 100th. More specifically, biennial, as oppposed to annual, budgets should be developed to provide budget makers with more time to refine their projections. A biennial budget would grant authorizing and appropriating committees greater discretion and lead time in meeting budget guidelines. A two-year budget cycle would also give the business community a better sense of the government's outlook for the next 24 months.

5. Liability Reform. The liability insurance crisis must be resolved. The elements of a solution seem to include:

- Acknowledging that the hazards of everyday living will always be among us.
- Returning to a fault-based standard of liability.
- Continuing punitive damages in cases of deliberate corporate misconduct; amounts awarded should be divided equally between plaintiffs and an appropriate state agency or program.
- Establishing nationally uniform product and commercial liability standards, including liability based on scientific knowledge at the time of manufacture, not at the time of injury.
- Limiting attorneys' contingency fees.
- Developing standards for insurance companies to disclose the terms and conditions of their portfolios and their lines of insurance. The insurance industry should do so itself before the government is forced to step in.

> ***Every problem should not require a legal remedy.***
>
> **Bruce Bunner**
> **Insurance Commissioner**
> **State of California**

6. Small Business and Taxes. The House Ways and Means Committee and the Senate Finance Committee should analyze the impact of all new tax legislation on small business. These analyses should include statements of the assumptions, rationales, and data underlying the analyses.

7. Streamlining Procedures. State and local governments should streamline the many procedures governing the establishment and operation of a business. We believe that a single office responsible for helping entrepreneurs and small businesses complete the paperwork requirements for getting started can be helpful. These offices can also serve as both ombudsmen and advocates for small business.

8. The Small Business Administration. The Small Business Administration has evolved over 30 years in response to the needs of the small business commmunity. Despite the limited resources at its disposal in the face of sweeping responsibilities, the SBA has made significant contributions to small business through its creation of the venture capital network and of certified local development companies, as well as its loan guarantee programs, management assistance, and advocacy. We believe this record should be respected, and that the SBA, without diluting its mission or independence, can be made more effective by:

- refocusing its lending efforts to help develop the systems, institutions, and credit instruments needed by the small business community;
- exerting ongoing, not sporadic, leadership to help states and localities focus on small business as a foundation of their economic development; and
- expanding and improving SBA's advocacy role for small business, including its ability to analyze small business growth.

> ***I want to pay my fair share of taxes but I cannot plan growth intelligently when taxing policies are so volatile.***
>
> **Earl Hess**
> **Lancaster Laboratories**
> **Lancaster, Pennsylvania**

9. Labor-Management Relations. We recommend a White House conference on labor-management relations to help encourage a positive culture for business development and employee relations. The White House can direct the nation's attention to the imperative for new ways of thinking about the relationships between business and labor in the new competitive environment. We need partnerships between management and labor, taking into account new management styles and changes in employee expectations. Such innovations as more joint planning and diagnosis, work teams, task delegation, reconciling seniority with ability, pay differentials, and training incentives should be considered.

A Competitive People

A competitive people defines itself in the challenges it meets—and overcomes. In former years, Americans passed that test on the frontier, in the crucible of political and industrial revolutions, and in the necessity of battle. In our own time, we have pushed back the boundaries of science and technology.

Now another challenge lies before us—pursuing our national aspirations in the context of the new world economy. We believe that today's Americans are up to the task. Made aware of the dimensions of the problem, they will work as hard as those who tamed the wilderness, they will save as much as those who financed World War II with war bonds, and they will learn what they need to know in order to participate productively in the economic struggle we face.

> ***Indians like to think they can soar like eagles. Entrepreneurship permits us to maintain that vision.***
>
> **Robert Powless**
> **President**
> **Mount Senario College**

In taking up this challenge, we have little tolerance for those who counsel patience. To those who point to every imaginable excuse to explain the American decline, we say our country has lost world market shares in good times and bad, on the back of a strong dollar and a weak one. We agree that the growth of services and information industries is significant and must be maintained, but we insist that an America stripped of its industrial and manufacturing foundation is inconceivable. The Commission has no desire to deny to the people of other lands the higher standards of living and material well-being their economic success deserves; but we are equally convinced their success does not require us to sacrifice the well-being of American workers and families.

Nor is the Commission's conviction about the importance of small business to be interpreted as lack of concern while one great American industry after another falls before foreign competition. Reversing the decline in the fortunes of our large corporations is a compelling national need and critically important to the many small firms which provide the products, parts, and services to our nation's industries.

We call on all who care about our future to step forward to meet this latest in a long line of challenges. All will be tempered by it; none will be untouched by it; mastering it will be the making of our future.

To our public officials: We urge you to take seriously the findings in this report and to respond promptly by enacting the recommendations that fall within your areas of responsibility. Of particular importance is your steadfast commitment, in the face of short-term pressures from all sides, to the long-term interest of American competitiveness.

To our citizens, including parents, students, and employees: Act now on the realization that the traditional structure of employment and job security is becoming a thing of the past. Honing individual skills will give each of us a competitive edge in the future.

To our corporate officials: We remind you that the freedom to engage in business carries with it the obligation to lead, to respond to the public interest in making decisions about plant locations and investment opportunities. Most important, your actions must affirm, not undermine, the dignity of employment. You have a special responsibility to take seriously the imperative for retooling, marketing abroad, controlling costs, and thinking strategically for the long haul rather than tactically for the short.

To our financiers and bankers: You have a central role to play in creating the financial processes and instruments that will, in partnership with the public sector, promote foreign trade, encourage small business expansion, and lead business owners to productive participation in these efforts.

To our labor leaders: Share with the members of your unions your realization that the welfare of your members depends on a competitive economy. Just as collective bargaining has been the heart of trade unionism in the past, productivity will be its soul in the future.

We speak finally to our small business men and women, the owners and entrepreneurs who have carried the American workforce safely through the difficult last decade: Maintain your belief in yourself. Build on your accomplishments. Push back your horizons. Above all, hold fast to your dreams, remembering that they sustain not only you but all of us.

Appendices

Appendix A

Acknowledgments

Many people and organizations made the work of this Commission possible; we cannot overstate the value of their contributions.

The Commission wants, in particular, to acknowledge its debt to the following:

- The 38th and 39th Presidents of the United States who lent us their support.
- The 18 members of the House and Senate who conceived of the Commission and saw it to fruition.
- The Charles Stewart Mott Foundation, Flint, Michigan, which provided the initial financial and conceptual support for the Commission and more than half of its financial resources. Jack Litzenberg of the foundation's staff, assisted by Ruth Goins, was an unfailing source of encouragement during the Commission's existence.
- The Andrew W. Mellon, John D. and Catherine T. MacArthur, and Rockefeller foundations as well as the Carnegie Forum on Education and the Economy of the Carnegie Corporation of New York, which also provided essential financial support to our efforts.
- Many organizations and institutions which provided us with meeting space, logistical and other support to help extend the Commission's resources, including the Gerald R. Ford Library, Ann Arbor, Michigan; the Carter Center of Emory University, Atlanta, Georgia; the Bank of America, San Francisco, California; Federal Hall National Memorial, New York City; Rainier National Bank, Seattle, Washington; Control Data Corporation, San Antonio, Texas; the Chamber of Commerce, San Francisco, California; and the New York Stock Exchange.
- The many organizations representing small business that provided us with the benefit of their experience and knowledge, including the U.S. Chamber of Commerce, the National Federation of Independent Business, Small Business United, the National Association of Women Business Owners, the National Association of Small Business Investment Companies, the Small Business Administration, the White House Conference on Small Business and its staff, the Corporation for Enterprise Development, and the National Small Business Association.

- The witnesses and experts who, often at great expense to themselves, eloquently made their cases before the Commission.
- The businesses and organizations from which the Commissioners were drawn, and which supported their time and often their expenses in pursuit of this public endeavor, including the National Development Council, the Bank of America, the AFL-CIO, AT&T, Pacer Systems, Inc., Price Waterhouse, King & Spalding, the American Enterprise Institute, Alexander Haagen Development Company, and the National Business League.

We are especially grateful to Price Waterhouse, the A. Gary Shilling Company, New York University, and the AFL-CIO for the expert assistance members of their staffs provided the Commission. Robert Haddad of Price Waterhouse explored the idea of a mutual fund for small business. Roger Fulton of the Shilling Company provided a comprehensive report on economic developments affecting small firms and drew the declining purchasing power of American families to our attention. Lynne Brown of New York University attended many of our meetings and offered numerous suggestions for structuring and improving this report. Markley Roberts of the AFL-CIO proved an inexhaustible source of information and a careful and constructive critic of the report as it developed.

The Commission also wants to express its appreciation to the staff which helped it throughout its work. Alisa Pittrizzi, Audrey Gallagher, Satura Bridgewater, and Christine Gresock, at different times, helped organize our work.

In particular, we note the invaluable contributions of Kevin Urquhart: without his able and efficient help throughout, we would never have had meeting or hotel space, adequate travel arrangements or notice of meetings, nor have been able to expect prompt and cheerful turnaround on constantly changing agendas and report drafts.

We are indebted also to two consultants: Anne Paxton and Andrea Haines. Ms. Paxton provided summaries of each of the Commission's meetings as well as two newsletters reporting the Commission's work. Ms. Haines developed Appendix B, prepared the Commission's archives, and played an indispensable role in providing research assistance to the Commission.

Finally, we express our gratitude to two small firms that helped prepare this volume: Wordsmith, Inc. and Moonstruck Graphics, both in Virginia. Bruce Boston of the former proved a talented writer and editor, and Dan and Vicki McQuillen, of the latter, designed this report.

Appendix B

Annotations

A Debtor Nation

On September 14, 1986, Clyde Farnsworth wrote in *The New York Times*, "(After) serving as the world's creditor since World War I, the United States this year became the world's largest foreign debtor, overtaking Mexico and Brazil.... Because an increasing portion of America's wealth must go to pay the mounting foreign debt, the huge deficits threaten to lower living standards in this country."

Net U.S. International Position 1982-1985

(billions of dollars)

1982	+136.2
1983	88.5
1984	4.4
1985	-107.4

Source: Department of Commerce, Bureau of Economic Analysis, *Survey of Current Business*, June 1986.

In June 1985, a major publication of the Department of Commerce (*United States Trade: Performance in 1984 and Outlook*) anticipated the reversal of the U.S. international position:

"The recent large U.S. trade deficits demonstrate that the United States has been consuming significantly more than it is producing and borrowing abroad to make up the difference.... Sometime in 1985 the United States will officially become a net debtor nation for the first time since 1914. In other words, the United States will owe more to foreigners than they owe to the United States.... This would represent an enormous swing... in the U.S. net international position—from largest creditor nation to largest debtor nation—in only four years.

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"This foreign debt will have to be serviced. The United States will become a net interest payer to foreigners, rather than a net interest recipient. Moreover, at some point, foreigners will no longer be willing to continue enlarging the U.S. net debtor position. At that point, the United States will have to switch from consuming more than it produces to consuming less than it produces in order to make interest payments on the debt. That is, a portion of what is produced in the United States will not be available for domestic consumption or investment but will have to be exported to earn foreign currency to service accumulated foreign debt.

"When this switch occurs, it may have undesirable effects on the availability of investment capital, interest rates, U.S. economic growth, and the U.S. standard of living."

Exports

According to the International Trade Administration, U.S. Department of Commerce (June 1985), the U.S. share of world merchandise exports fell from 18 percent in 1960 to 11 percent in 1984. The President's Commission on Industrial Competitiveness, *Global Competition: The New Reality* (January 1985) reports the same findings. According to the Department of Commerce, U.S. exports of manufactured goods fell from $166.8 billion in 1981 to $162.0 billion in 1985.

The International Trade Administration also reports that the U.S. high-tech trade surplus dropped from $26.6 billion in 1980 to $6.2 billion in 1984. A report prepared for the Joint Economic Committee (*The U.S. Trade Position in High Technology: 1980-1986*, October 1986) predicts that U.S. high-technology trade will show a deficit of about $2.6 billion in 1986.

Agricultural trade accounts registered a deficit in May, June, and July of 1986, according to the International Economics Division of the Department of Agriculture (October 1986).

Productivity

American output per hour of all persons increased, on average, 2.4 percent in the 1960s, 1.1 percent in the 1970s, and 0.8 percent from 1980-1985 (*Economic Report of the President*, 1986).

Economist A. Gary Shilling attributes the slowdown to the influx of inexperienced baby boomers into the labor force, depressed capital spending, inflation, and, in the 1970s, a decline in the work ethic ("The World Has Definitely Changed," August 1986).

Brookings Institution economist Barry Bosworth concludes that the causes of the post-1973 slowdown "remain, in large part, a mystery" (*Tax Incentives and Economic Growth*, The Brookings Institution, Washington, D.C., 1984, p. 177).

Growth of the Deficit

As the annual federal deficit has increased, so too have the national debt and annual interest payments on the debt.

Federal Debt, Deficits, and Interest Payments 1960-1985

Year	Gross Federal Debt ($ billion)	Annual Surplus (+) or Deficit (-) ($ billion)*	Interest on Gross Federal Debt ($ billion)	Interest as Percentage of Federal Outlays (%)
1960	290.9	+0.3	9.5	8.7
1970	382.6	-2.8	20.0	8.0
1980	914.3	-73.8	75.2	10.2
1981	1,003.9	-78.9	96.0	11.6
1982	1,147.0	-127.9	117.5	13.1
1983	1,381.9	-207.8	128.9	13.3
1984	1,576.7	-185.3	154.1	15.1
1985	1,827.5	-212.3	179.4	15.6

*Includes total receipts and outlays, budget and off-budget.

Source: Office of Management and Budget, *The Budget for Fiscal Year 1987*. Various tables from *Special Analyses* and *Historical Tables*.

Income

Several sources point to declining purchasing power and real (i.e., inflation-adjusted) income for American workers and families:

Average Gross Weekly Earnings for Production and Non-Supervisory Workers in Constant 1977 Dollars

1972	$198.41
1977	189.00
1985	171.60

Source: *Economic Report of the President*, 1986

Index of Adjusted* Hourly Earnings of Production and Non-Supervisory Workers in Constant 1977 Dollars

(1977 = 100)

1972	101.2
1977	100.0
1985	94.3

Source: *Economic Report of the President*, 1986. (*Adjusted for overtime and inter-industry employment shifts.)

Index of Real Compensation* Per Hour for all Workers in Non-Farm Business

(1977 = 100)

1972	95.7
1977	100.0
1985	98.2

Source: *Economic Report of the President*, 1986. (*Hourly compensation divided by Consumer Price Index. Hourly compensation includes employees' wages and salaries and employers' contributions for benefits.)

(See table, P. 51, "Real Average Weekly Wage for Non-Supervisory Workers by Industry.")

According to Harvard's Bruce R. Scott, speaking at the Commission's first meeting, real per capita "spendable" earnings of American workers have been declining since 1972, although "per capita income" has risen. He explains that four factors account for this phenomenon: "increased participation in the labor force, the creation of a large number of low-paying service jobs, dramatic increases in real incomes for those not working (for example those on social security), and the increased fraction of worker incomes absorbed by income and social security taxes." (See Scott, Bruce R., and George C. Lodge (eds.), *U.S. Competitiveness in the World Economy*, Boston: Harvard Business School Press, 1985.)

Loss of High-Wage Jobs

The Bureau of Labor Statistics documents the decline in manufacturing jobs. In 1980, there were 14.2 million manufacturing production workers. By June 1986 the number of such workers had dropped to 13.1 million, for a loss of 1.1 million jobs (Department of Labor, Bureau of Labor Statistics, *Employment and Earnings*, July 1986). Total employment in services rose four million, from 17.9 million in 1980 to 21.9 million in 1985 (*Economic Report of the President*, 1986).

Average gross weekly earnings (current dollars) for manufacturing workers in 1985 were $385.97, about 50 percent higher than the $256.43 weekly earnings for service workers.

(See tables, pp. 52-53, "Full and Part-Time Employees on Private, Nonagricultural Payrolls, 1950–1985.")

Real Average Weekly Wage for Non-Supervisory Workers by Industry

(BLS Report—1967 $)

	Mining	Construction	Manufacturing	Transportation & Public Utilities	Wholesale Trade	Retail Trade	Finance Insurance Real Estate	Services
1973	$151	$177	$125	$153	$120	$ 72	$ 97	$ 88
1978	$170	$163	$128	$155	$117	$ 67	$ 91	$ 84
1984	$162	$147	$120	$141	$111	$ 57	$ 89	$ 81
1985	$160	$141	$121	$140	$111	$ 54	$ 90	$ 81

Source: A. Gary Shilling and Company, "The World Has Definitely Changed," August 1986.

Full and Part-Time Employees on Private, Nonagricultural Payrolls[1] 1950-1985

	Total Employment		Goods-Producing Industries[2]			Service-Producing Industries[3]		
Year	Emp. (000)	Average Weekly Earnings[4]	Emp. (000)	% of Total Emp.	Average Weekly Earnings[4]	Emp. (000)	% of Total Emp.	Average Weekly Earnings[4]
1950	34,349	$133.83	15,440	45	$151.83	18,909	55	N.A.
1960	38,516	164.97	15,653	41	192.11	22,863	59	N.A.
1970	48,156	186.94	17,506	36	225.88	30,649	64	$164.58
1980	60,331	172.74	18,398	30	226.16	41,933	70	149.08
1985	65,911	171.60	17,551	27	232.18	48,360	73	147.49

Source: U.S. Department of Labor, Bureau of Labor Statistics, *Employment, Hours, and Earnings, United States, 1909-1984*, May 1985; *Employment and Earnings*, February 1986; *Economic Report of the President*, February 1986.

1. Includes all production or nonsupervisory employees, but not supervisors, managers, proprietors, executives, the self-employed, or domestic workers.

2. Includes manufacturing of durable and nondurable goods, mining, and construction.

3. Includes transportation and public utilities; wholesale trade; retail trade; finance, insurance, and real estate; and services (e.g., hotels, personal services, business services, auto repair, motion pictures, amusement and recreation, health care, legal and other professional services such as engineering, architecture, and accounting).

4. Constant 1977 dollars. Earnings for goods-producing and service-producing industries calculated by Commission staff according to BLS weighting formulas.

Full and Part-Time Employees On Private, Nonagricultural Payrolls [1]
Selected Industries 1950-1985

	Goods-Producing Industries			Service-Producing Industries					
	Manufacturing			Retail Trade			Services		
Year	Emp. (000)	% of Total Emp.	Average Weekly Earnings [2]	Emp. (000)	% of Total Emp.	Average Weekly Earnings [2]	Emp. (000)	% of Total Emp.	Average Weekly Earnings [2]
1950	12,523	36	$146.80	6,375	19	$100.03	N.A.	N.A.	N.A.
1960	12,586	33	183.48	7,627	20	118.12	N.A.	N.A.	N.A.
1970	14,044	29	208.00	10,046	21	128.66	10,481	22	$150.80
1980	14,214	24	212.06	13,500	22	108.29	15,921	26	140.12
1985	13,215	20	219.93	15,560	24	99.51	19,366	29	146.11

Source: U.S. Department of Labor, Bureau of Labor Statistics, *Employment, Hours, and Earnings, United States, 1909-1984*, May 1985; *Employment and Earnings*, February 1986; *Economic Report of the President*, February 1986.

1. Includes all production or nonsupervisory workers, but not supervisors, managers, proprietors, executives, the self-employed, or domestic workers.

2. Constant 1977 dollars.

Unemployment

Average Unemployment Rate, All Civilian Workers

1950-1959	4.5 percent
1960-1969	4.8 percent
1970-1979	6.2 percent
1980-1985	8.1 percent

Source: U.S. Department of Labor, Bureau of Labor Statistics, in *Economic Report of the President*, 1986.

Automobiles

Hiroyasu Ono, executive vice president of Toyota, estimates that Japanese automakers in the U.S. will produce 1.2-1.3 million cars in 1988, equal to the production of passenger cars by the third-largest domestic automaker in 1984 (Interview, *Journal of Japanese Trade and Industry*, Number 6, 1985). In 1985, the Japanese share of the U.S. domestic auto market was 23.5 percent (*U.S. Industrial Outlook 1986*). The April 22, 1985 *Business Week* includes predictions that all automobile imports will account for 40 percent of U.S. sales by 1990.

Consumer Electronics

The Department of Commerce publication *U.S. Industrial Outlook 1986* documents declines in U.S. manufacture of televisions and radios. Moreover, according to the Department of Commerce, employment in the consumer electronics industry dropped from 76,700 in 1978 to 45,300 in 1983 (*U.S. Industrial Outlook 1986*).

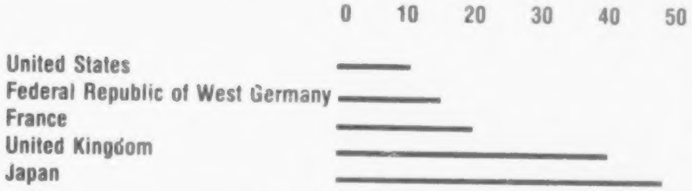
Manufactured Products

Bruce R. Scott and Undersecretary of Commerce Clarence Brown told the Commission at its first meeting that 70 percent of American manufactured products are subject to foreign competition, a situation confirmed by the President's Commission on Industrial Competitiveness (*Global Competition: The New Reality*, January 1985).

In their book, *Subsidies in International Trade* (Washington, D.C.: Institute for International Economics, 1984), Gary Clyde Hufbauer and Joanna Shelton Erb show official export credit authorizations for seven nations. Japan's total exceeds U.S. spending by a factor of four.

A Comparison of Total Exports Supported by Official Finance in the Major Trading Nations in FY 1982

(billions of dollars)



Source: The President's Task Force on International Private Enterprise: Report to the President, December 1984, p. 91.

Steel and Textiles

The U.S. Department of Commerce (*U.S. Industrial Outlook 1986*) reports that imports accounted for 26.2 percent of the U.S steel market during the first half of 1985. The American Iron and Steel Institute reports that the U.S. share of world crude steel output dropped from 131.5 million tons in 1970 to 92.5 million tons in 1984 (*AISI Annual Statistical Report,* 1985).

In 1984 alone, imports of textiles rose more than 40 percent. U.S. imports of textiles and apparel from Hong Kong, Singapore, Taiwan, and South Korea increased from $4.8 billion in 1980 to $9.3 billion in 1984. These countries account for approximately 60 percent of U.S. clothing imports (U.S. Department of Commerce, *United States Trade: Performance in 1984 and Outlook,* June 1985).

Trade Deficits

The *Economic Report of the President* (1986), reports that the U.S. balance of merchandise trade has been negative in all years since 1971 except 1973 and 1975. In constant dollars, U.S. exports of goods and services declined over the period 1980-1984 at a 2.1 percent annual rate, while imports rose ten percent annually. The U.S. current account, the broadest measure of U.S. trade in goods and services, recorded record deficits in the first three quarters of 1986 (*The Washington Post*, December 17, 1986).

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The Spirit of Enterprise

There is no single measure of new business formation. Analysts agree that the data on new business incorporations quoted here probably overstate the number of new businesses, since the data include incorporations or internal realignments of existing firms. The Dun & Bradstreet series on business starts reports the number of new entries to

D&B's commercial credit information file, and, since it excludes businesses not in the credit market, may understate the number of new firms. Business starts in the first half of 1986 rose 8.4 percent over the same period in 1985 to 129,035, accounting for an estimated 638,465 new jobs (*Dun & Bradstreet Looks at Business*, September/October 1986).

Average Annual New Business Incorporations 1950-1985

1950-1959	125,024
1960-1969	205,159
1970-1979	365,898
1980-1985	597,736

Source: Department of Commerce, Bureau of Economic Analysis.

Increases in self-employment parallel increases in new businesses. The 1986 small business report of the President shows that the number of unincorporated, self-employed persons increased almost 50 percent between 1970 and 1984. Over the same period, the number of wage and salary workers grew 35 percent, and the civilian labor force increased by 37 percent.

D&B reports that firms with fewer than 100 employees were expected to generate two million of the three million new jobs in 1986. The highest rate of job generation is in the smallest firms (1-19 employees)—they were expected to contribute 31.9 percent of all new jobs in 1986 (*Dun & Bradstreet Looks at Business*, May/June 1986).

Ability to Diversify Economic Opportunity

The information on women-owned businesses was presented to the Commission by the National Association of Women Business Owners. A similar assessment of the progress of women-owned firms is contained in *Small Business in America: The Year 2000 and Beyond* (1986), prepared by the Naisbitt Group for the Institute for Enterprise Advancement of the National Federation of Independent Business. That report also includes figures on Hispanic-owned businesses from the Department of Commerce.

The number of black-owned businesses increased from 231,203 in 1977 to 339,239 in 1982, according to the SBA (*The State of Small Business*, 1986). Because employment in black-owned firms declined slightly over that period, analysts suggest that much of the growth in black-owned businesses represented self-employed entrepreneurs with few or no employees.

A Simple Prescription

Dr. Birch met with the Commission on September 11, 1985. He expanded on his 1981 article ("Who Creates Jobs?" *The Public Interest*, Fall 1981) in which he suggested that innovative small firms are the leading edge of a shift in the American economy from being based on hardware to being based on "thoughtware." In that article he wrote: "Every area in the United States seems to lose jobs at about the same rate, regardless of how rapidly the net job pool is expanding or contracting. . . . An eight percent loss every year means that half of an area's jobs and establishments must be replaced every five years for the area simply to break even."

Rebecca J. Heflin of the Texas Economic Development Commission testified before the Commission about the job creation task facing the state.

According to the Alabama Department of Industrial Relations (May 1986), Birmingham employment in primary metals declined from 24,200 in 1975 to 13,000 in 1985, while employment in services increased 43 percent, from 53,000 to 81,000.

The Massachusetts data were provided in a 1985 study, "Economic Revitalization and Job Creation in America's Oldest Industrialized Region," by James H. Howell of the Bank of Boston and Linda D. Frankel of the Council for Economic Action in Boston.

Functional Illiteracy

Illiteracy estimates vary greatly. A report by the National Assessment of Educational Progress, "Literacy: Profiles of America's Young Adults" (1985) sets ten million as the upper limit of the number of illiterate Americans. The Coalition for Literacy puts the number at 27 million Americans—about one adult in five. The professional journal of the American Association of Occupational Health Nurses (1986) estimates that 35 million Americans cannot read, and an additional 30-40 million cannot read well enough to understand safety warnings on the job.

Skills of Secondary School Graduates

See, for example, the reports of the National Commission on Excellence in Education (*A Nation at Risk*, April 1983), of the Carnegie Forum on Education and the Economy (*A Nation Prepared*, 1986), and of the National Assessment of Educational Progress (November 1986).

No Coherent Training Policy

According to the National Conference of State Legislatures, 14 different training programs have been adopted and abandoned since 1962.

Elaine Malek told the Commission in San Francisco that private sector involvement in publicly supported employment efforts is hindered by legislative provisions prohibiting wage subsidies for private employers and requiring advance commitments to hire trainees.

Engineering Shortage

Data from the National Research Council of the National Academy of Sciences show that foreign students account for 52.9 percent of engineering enrollment. See also National Science Foundation, *Academic Science Engineering Graduate Enrollment and Support*, Washington, D.C., 1983.

Wassily Leontief

See Leontief, Wassily, and Faye Duchin. *The Future Impact of Automation on Workers*. New York: Oxford University Press, 1986. The number 15 million which appears in the text is a Commission staff estimate based on the analyses presented, but the number itself does not appear in the volume. However, in a telephone conversation with the Commission staff director in October 1986, Faye Duchin agreed that the number is a reasonable estimate of the shortage of skilled workers based on the most likely projections of the rate of business acquisition of new technologies.

New Competitive Environment

The Department of Commerce reports that less than ten percent of the 376,000 manufacturers in the United States export their products.

During their working life, most individuals work for an average of ten different employers, according to economist Robert Hall ("The Importance of Lifetime Jobs in the U.S. Economy," *American Economic Review*, September 1982). A 1983 study for the Department of Commerce found that the median job tenure for men was four years, and for women, 2.5 years.

The number of high school students studying a foreign language in school has declined since the 1960s. Less than one quarter of the student population was enrolled in a foreign language course in 1982. Degrees earned in foreign languages (B.A., M.A., Ph.D.) fell by over 50 percent between 1971 and 1983 (National Center for Education Statistics, U.S. Department of Education, *Statistical Abstract*, 1986).

No Understanding of Entrepreneurship

University of Michigan political scientist John Jackson's research on public perceptions of entrepreneurs was issued in June 1986, and widely reported in the public and business press. He concluded that although entrepreneurs and small businesses create most of the jobs in the United States, most of his national sample of 1,000 people were not aware of this fact.

Lack of Knowledge of Economics

Periodic surveys by the Joint Council on Economic Education, including its "Test of Economic Literacy" (1986), indicate that most high school students do not understand how the free enterprise system works.

Several reports from the Joint Council also document the lack of public awareness about economic matters.

Educators Equally Uninformed

Data from the Joint Council on Economic Education indicate that only eight percent of American teachers studied economics as undergraduates, and that most adults cite television as their main source of information on the economy. In the July 9, 1986 *Wall Street Journal*, Nobel Laureate James Tobin of Yale cited a report of the Southern Regional Education Board showing that only one quarter of teachers had studied economics, and the Rhode Island Council of Economic Education reports that only six percent of its teachers ever had a course in economics.

Savings

At the Commission's first meeting in September 1985, these figures were cited by Bruce R. Scott. According to the Department of Commerce publication "International Economic Indicators," the savings rates of West Germany, Canada, and France are twice the U.S. rate; Japan's savings rate is over three times the U.S. rate.

Harvard economist Benjamin M. Friedman notes that continued federal deficits in the range of four to six percent of GNP "will absorb more than half of the private sector's normal net savings" ("Saving, Investment, and Government Deficits," in Scott, *U.S. Competitiveness*, 1985).

Cost of Capital

George Hatsopoulos made an issue of the cost of capital at the New York hearing in June. He prepared a paper entitled "The Cost of Capital," documenting capital costs for the President's Commission on Industrial Competitiveness (October 1984).

D. Bruce Merrifield, assistant secretary for productivity, technology, and innovation at the U.S. Commerce Department, asserts that "the cost of capital in the United States is two to three times higher than in Japan and other countries" ("Don't Ration Innovation," *Enterprise*, February 1985).

Use of Capital

Peter Behr reported this situation in a *Washington Post* article, January 12, 1986. The figures are from the Board of Governors, Federal Reserve System.

Edward L. Hennessey, Jr., chairman and CEO of Allied Corporation, attributes the recent merger upsurge to "merger bankers and lawyers who are overrewarded for dreaming up outlandish deals," and to the availability of "junk bonds" requiring neither equity nor collateral.

These developments, he says, threaten "capital projects, R&D and other long-term programs. . . . (The) raiders' actions weaken U.S. business and undercut our competitiveness in international markets" (Speech, May 1985, Economic Club of Detroit).

Morgan Stanley economist Stephen S. Roach noted in a May 27, 1985 *Business Week* article that "we've reached the point where corporate debt loads are starting to impinge on capital spending programs."

The Narrow Base of Capitalism

The Federal Reserve System reports that in 1983 only seven percent of all families had a brokerage account, 17 percent had an IRA or Keogh account, and 14 percent had money market accounts. Representative Stan Lundine (D-N.Y.) cited the statistics on stock ownership in a 1984 Congressional economic conference, noting that the lack of widespread ownership is a "major concern" (Joint Economic Commitee and the Congressional Clearinghouse on the Future, *The New Economy: Proceedings of a Congressional Economic Conference*, June 1984).

Aging Equipment

Senator Slade Gorton (R-Wash.) cited these statistics in a 1983 Senate hearing (Committee on Science, Technology, and Space, *Hearing on S.1286: The Role of Technology in Promoting Industrial Competitiveness*, Seattle, November 23, 1983).

Data from the Bureau of Economic Analysis, Department of Commerce (unpublished data, October 1986), confirm that manufacturing equipment in America is becoming older: despite increased expenditures on "durable equipment" in the 1980s, the average age of manufacturing equipment increased from 8.4 years in 1980 to 8.9 years in 1985. This average obscures industry differences: the average age of equipment in primary metals industries is now nearly 13 years; in electronics, by contrast, it is 6.8.

Several other trends are clear from the information available: (1) Business spending on "durable equipment" has increased by over one third since 1982 (Commerce, *Survey of Current Business*, July 1986). (2) Manufacturers are, for the most part, modernizing existing facilities, not expanding capacity (1985 survey of capital spending plans by McGraw-Hill, Inc.). (3) A major portion of the overall increase in expenditures for "durable equipment" has been devoted to acquiring information processing and not manufacturing equipment. Expenditures on information processing and related equipment increased 41 percent between 1982 and 1985 while industrial equipment expenditures increased 18 percent (Commerce, *Survey of Current Business*, July 1986).

Consumer Debt

Total installment consumer credit, excluding mortgages, was $577 billion in August 1986. According to the Federal Reserve, consumer credit outstanding at the end of 1976 stood at $190.7 billion. *The Wall Street Journal* reported on September 10, 1986 that consumer credit at the end of July 1986 was 14.6 percent higher than during the same period in 1985.

Venture Capital

A 1984 study prepared for the Joint Economic Committee (*Venture Capital and Innovation*) concluded that venture capital firms fund only five percent of the proposals submitted to them, and "only the cream of the crop of entrepreneurial investments receive funding from the venture capital community."

According to *The State of Small Business* (1986), organized venture capital firms "are bypassing smaller deals—those under $400,000." Don L. Gevirtz, chairman and CEO of the Foothill Group, Inc., wrote in 1985 that venture capital has become "almost unavailable" for most companies (*Enterprise*, February 1985).

Despite rapid growth in annual venture capital investment (over $2.5 billion in 1985, according to Venture Economics, Inc.), venture capital firms are "typically not interested" in small start-up ventures, says David Ellsbury of Deloitte Haskins & Sells in Boston (*D&B Reports*, May/June 1986). Small companies that do not show promise of immediate high returns and a good chance of either being acquired or going public within a few years stand little chance in the venture capital market.

Long-Term Financing Difficult

According to the President's 1984 *Report on the State of Small Business*, small firms obtain 39 percent of their funds from external sources; by contrast, large firms raise over 57 percent of their funds outside the firm.

The Federal Reserve System Board of Governors reports in *The State of Small Business* (1986) that the percentage of long-term bank loans used for small loans (under $100,000) declined from 19 percent in August 1979 to 12 percent in May 1985. Similar results were reported in a survey of the National Federation of Independent Business, "Small Business and Credit" (July 1984).

In 1983, the National Federation of Independent Business reported on two nearly identical surveys on banks and commercial credit. The study described the terms of small business loans from banks:

- Ninety-nine percent of loans to small business exceed the prime rate, on average by three percentage points.
- Nearly half (47 percent) of small business loans are for 12 months or less with an average maturity of six months; only 13 percent are for 61 months or more.

Collateral is required to secure most of these loans—50 percent of the short-term and 90 percent of the long-term loans have collateral requirements—and many loans involve a combination of personal and business assets as collateral.

Bias Against Small Business Investment

A 1985 study issued by Congressman Daniel E. Lungren (R-Calif.) on behalf of the Joint Economic Committee investigated the "alleged capital gap" facing small business.

On the basis of its survey of Small Business Investment Companies (SBICs), the committee concluded that small business is discriminated against in capital markets:

- Seventy-two percent of Small Business Investment Company managers, 64 percent of independent venture capitalists, and a majority of corporate venture managers agreed that "institutional investors, including banks, have a bias against investing in small business."
- They listed as the major reasons for the bias:
  - —lack of institutional expertise;
  - —excessive avoidance of risk;
  - —high portfolio costs associated with an active effort to help small business;
  - —inadequate secondary markets for small business loans; and
  - —inadequate risk-adjusted returns.

Raising Equity

Equity markets involve substantial, upfront legal and accounting costs for both public offerings (registered with the SEC and probably advertised) or private offerings (not registered and not permitted general solicitation). Both offerings require a formal offering document.

The SEC has been quite active in trying to minimize the burdens of these procedures on small firms—it holds an annual SEC Small Business Capital Formation Forum, and in 1979 approved a simplified registration form for small public offerings, S-18. In 1982, it adopted Regulation D, a set of three exemptions governing private offerings.

Impact on Minorities

Earl Graves, editor of *Black Enterprise*, provided ample evidence of the problems of minority small business owners at the Commission's New York hearings. Studies from the Brookings Institution, the Small Business Administration, and the National Federation of Independent Business document the importance of community resources and personal savings in starting small firms and the difficulties minority entrepreneurs face as a consequence. For example, the President's 1984 report on small business points out that the "median 1982 family income of blacks and persons of Spanish origin was 58 percent and 69 percent, respectively, of the median income of all races," and observes, "This condition limits the prospects of these families to accumulate savings to finance business undertakings."

Few Exporters

The President's Commission on Industrial Competitiveness reported in January 1985 that "250 firms account for nearly 85 percent of all U.S. exports." The export potential of small firms was stressed in testimony before the Commission by Michael Czinkota of Georgetown University. Statistics from the Department of Commerce on the export activities of American firms (1981) show that 12.8 percent of manufacturing employment is export-related.

Export Decline

Arthur Domike testified before the Commission in Atlanta on export decline. Between 1980 and 1982, U.S. merchandise exports fell from $224.3 billion to $211.2 billion (*Economic Report of the President,* 1986).

Lack of Government Assistance

In December 1984, the President's Task Force on International Private Enterprise listed some of the mechanisms foreign governments use to promote exports:

"Financing of local currency costs for turnkey projects; inflation insurance for large contracts requiring long construction periods; exchange risk insurance for foreign currency-denominated loans; mixed credits that combine concessional government funds with commercial funds to produce lower than market-based interest rates and more lenient loan terms for exporters; and tied-aid credits that utilize the government's foreign assistance programs to influence procurement decisions in their exporters' favor. . . ."

Thus, increasingly, U.S. exporters find themselves having to compete against the national treasuries of mercantilist nations.

The task force concluded that the absence of U.S. government support of a similar nature "diminishes opportunities for U.S. private companies, especially small- and medium-sized, to participate in the LDC development process" (*The President's Task Force on International Private Enterprise: A Report to the President*, December 1984, p. 91).

Small Business Administration statistics were cited by Arthur Domike, vice president of Developing Systems, Limited, in testimony before the Commission, August 4, 1986. (The testimony was reported in the Bureau of National Affairs publication, *Daily Labor Report*, August 6, 1986.)

Appendix C

Schedule of Commission Events

The proceedings of these meetings, including the written testimony presented to the Commission, will be available through the National Technical Information Service (NTIS), Department of Commerce, after March 1987.

Commission Meetings

September 10-11, 1985
Washington, D.C.

November 18-19, 1985
Washington, D.C.

February 10, 1986
San Antonio, Texas

September 15, 1986
Seattle, Washington

November 7, 1986
Washington, D.C.

Commission Hearings

December 9, 1985 **Gerald R. Ford Library**
Ann Arbor, Michigan

- *Entrepreneurship*
- *Innovation, Technology, and R&D*

March 14, 1986 **Bank of America**
San Francisco, California

- *Education and Training*
- *Legal and Regulatory Environment for Small Business*

June 9, 1986 **Federal Hall National Memorial**
New York, New York

- *The Economic Outlook*
- *Capital Availability for Small Business*

August 4, 1986 **Carter Center of Emory University**
Atlanta, Georgia

- *Small Business and Exports*
- *International Comparisons*

Appendix D

Meeting and Hearing Testimony

First Meeting September 10-11, 1985 Washington, D.C.

Speakers

The Honorable Clarence J. Brown
Deputy Secretary
Department of Commerce
Topic: International Competitiveness

Bruce R. Scott
Professor
Harvard University
Graduate School of Business Administration
Topic: U.S. Competitiveness in the World Economy

The Honorable Don Ritter
U.S. House of Representatives
Topic: Targeting the Process of Innovation

George Gilder
Author
The Spirit of Enterprise
Topic: The Entrepreneurial Spirit

David Birch
Massachusetts Institute of Technology
Topic: Who Creates Jobs?

Second Meeting November 18-19, 1985 Washington, D.C.

Speakers

Michael Novak
Resident Scholar
American Enterprise Institute
Topic: Spirit of Democratic Capitalism

The Honorable John J. LaFalce
U.S. House of Representatives
Topic: Industrial Policy

Panels

Topic: The Small Business Agenda

Sam Hope
President-Elect
Small Business United
Milwaukee, Wisconsin

Thomas Donley
Director, Small Business Center
U.S. Chamber of Commerce
Washington, D.C.

Walter Stults
President
National Association of Small Business Investment Companies
Washington, D.C.

Virginia Littlejohn
Past-President
National Association of Women Business Owners
Washington, D.C.

Jerry Gulan
Executive Vice President
National Small Business Association
Washington, D. C.

Topic: Business Owners Speak

David Stewart
Partner
Miller, Cassidy, Larroca & Lewin
Washington, D.C.

James Lagos
Partner
Lagos & Lagos
Springfield, Ohio

Duane Pearsall
General Partner
Columbine Venture Fund, Inc.
Englewood, Colorado

Robert Haddad
Partner
Price Waterhouse & Company
Boston, Massachusetts

Earl Hess
President
Lancaster Laboratories
Lancaster, Pennsylvania

Third Meeting February 10, 1986 San Antonio, Texas
Hosted by the Business & Technology Center,
Control Data Corporation

Speakers

Jude Valdez
Executive Director
Center for Economic Development
University of Texas at San Antonio
Topic: Small Business Development Centers

Rebecca J. Heflin
Deputy Executive Director for Business Development
Texas Economic Development Commission
Austin, Texas
Topic: Small Business and Economic Development in Texas

Robert McKinley
Manager
Control Data Business & Technology Center
San Antonio, Texas
and
John D. Black
General Manager, Operations
Control Data Business & Technology Center
Minneapolis, Minnesota
Topic: Incubators and Job Creation

The Honorable Gary Hart
United States Senate
Washington, D.C.

Site Visits in San Antonio
Business & Technology Center
Mil-Tronics Corporation

Fourth Meeting September 15, 1986 Seattle, Washington
Hosted by Rainier National Bank

Speakers

John D. Mangels
President
Rainier National Bank
Seattle, Washington

The Honorable Rodney Chandler
U.S. House of Representatives
Washington, D.C.

Other Business
Discussion of Commission Report

Fifth Meeting November 7, 1986 Washington, D.C.

Speaker

The Honorable Parren J. Mitchell
U.S. House of Representatives
Washington, D.C.

Other Business
Discussion of Commission Report

First Hearing December 9, 1985 Ann Arbor, Michigan
Hosted by the Gerald R. Ford Library

Co-Chairs

Commissioner Camille Haney
Partner
Anderson, Benjamin, Read & Haney
Milwaukee, Wisconsin

Commissioner John Rennie
President
Pacer Systems, Inc.
Billerica, Massachusetts

Witnesses

Topic: Innovation, Technology, and Research and Development

Reed B. Harker
President
Michigan Research Corporation
Ann Arbor, Michigan

Robert Bailey
Director
Ohio Technology Transfer
Organization
Columbus, Ohio

Patrick A. Thompson
President
Trans-Matic
Holland, Michigan

Lawrence R. Crockett
Institute of Science & Technology
University of Michigan
Ann Arbor, Michigan

John Galles
Executive Director
Small Business Association of
Michigan
Detroit, Michigan

Todd Anuskiewicz
Research Director
Michigan Energy Research &
Resource Association
Detroit, Michigan

Topic: Entrepreneurship

Rodney Benson
President
Ann Arbor Chamber of Commerce
Ann Arbor, Michigan

Geri Larkin
Director, Office of New Enterprise
Services
Governor's Cabinet Council on Jobs
& Economic Development
Lansing, Michigan

Mary McCurry
President
National Association of Women
Business Owners
Denver, Colorado

Dwight Carlson
President
Perceptron
Farmington Hills, Michigan

William Schweke
Vice President
Corporation for Enterprise
Development
Washington, D.C.

Robert E. Powless
President
Mount Senario College
Ladysmith, Wisconsin

Philip Guyeskey
Manager, Small Business Programs
Michigan State Chamber of
Commerce
Lansing, Michigan

William Gleeson
Director, Center for the Study of
Entrepreneurship
Marquette University
Milwaukee, Wisconsin

Public Witnesses

Arthur Matthews
Donaldson & Donald
Detroit, Michigan

John Jackson
Institute for Social Research
University of Michigan
Ann Arbor, Michigan

Second Hearing March 14, 1986 San Francisco, California
Hosted by the Bank of America

Co-Chairs

Commissioner Shirley Chilton
Secretary of State & Consumer
Services
State of California
Sacramento, California

Commissioner Arthur V. Toupin
Vice Chairman of the Board
(Retired)
Bank of America
San Francisco, California

Witnesses

Topic: Education and Training

Luis David Corrales
Director
Chavez & Associates Institute
City of Commerce, California

Henry Levin
Institute for Research on Educational Finance & Governance
Stanford University
Stanford, California

Elaine J. Malek
Consultant
Elaine J. Malek Associates
Fond du Lac, Wisconsin

John M. Rankin
Executive Director
Goodwill Industries of the Inland Counties, Inc.
San Bernardino, California

Judy Semas
President
HOPE
San Jose, California

Nevzer Stacey
Office of Educational Research & Improvement
U.S. Department of Education
Washington, D.C.

William Turner
President
Technology Exchange Center
Garden Grove, California

Oscar Wright
Small Business Advocate
State of California
Sacramento, California

Topic: Legal and Regulatory Environment for Small Business

Bruce Bunner
Insurance Commissioner
State of California
San Francisco, California

Stephen Carroll
Deputy Director
Institute for Civil Justice
The Rand Corporation
Santa Monica, California

Walter Clemens
President, Western Division
Johnson & Higgins
San Francisco, California

Jaime Coira
Treasurer
Concord Engineering, Inc.
Richmond, California

Scott Hauge
Small Business Council
Chamber of Commerce
San Francisco, California

Walter Hoadley
Senior Research Fellow
Hoover Institution
Stanford University
Stanford, California

William P. Molmen
Vice President, State Programs
American Insurance Association
San Francisco, California

Richard M. Pennington
Senior Vice President
The Atlantic Companies
New York, New York

Public Witness

Paul Cramer
Realtor
San Francisco, California

Other Events in San Francisco

Breakfast meeting with San Francisco Chamber of Commerce

Third Hearing June 9, 1986 New York, New York
Hosted by Federal Hall National Memorial

Co-Chairs

Commissioner John Brademas
President
New York University
New York, New York

Commissioner Bernard E. Anderson
Wharton Center for Applied Research
Philadelphia, Pennsylvania

Witnesses

Topic: The Economic Outlook

Beatrice A. Fitzpatrick
President
American Woman's Economic Development Corporation
New York, New York

Peter Fousek
Executive Vice President & Director of Research
Federal Reserve Bank of New York
New York, New York

Roger H. Fulton
Director of Research
A. Gary Shilling & Company
New York, New York

Aaron Gurwitz
Vice President
Salomon Brothers
New York, New York

Ronald J. Moss
Commissioner
New York State Department of Commerce
New York, New York

Topic: Capital Availability for Small Business

Mark A. Bloomfield
President
American Council for Capital Formation
Washington, D.C.

Earl Graves
President & Editor
Black Enterprise Magazine
New York, New York

George N. Hatsopoulos
Chairman of the Board & President
Thermo Electron
Waltham, Massachusetts

Sara Loveland
Director
National Development Council
New York, New York

James Vitarello
President
James Vitarello Development Associates
Washington, D.C.

Other Events in New York

Lunch - Hosted by the New York Stock Exchange

Speaker: John Sloan, Jr.
President & Chief Executive Officer
National Federation of Independent Business
Washington, D.C.

Fourth Hearing August 4, 1986 Atlanta, Georgia
Hosted by the Carter Center of Emory University

Co-Chairs

Commissioner Richard Hammer
National Director, International Tax Services
Price Waterhouse & Company
New York, New York

Commissioner Robert Woodward
Partner
King & Spalding
Atlanta, Georgia

Witnesses

Topic: Small Business and Exports

Michael Czinkota
National Center for Export-Import Studies
Georgetown University
Washington, D.C.

Arthur Domike
Vice President
Developing Systems, Limited
Washington, D.C.

Edward J. Greenblat
Vice President
Chase Trade, Inc.
New York, New York

Carol Martel
International Department
Atlanta Chamber of Commerce
Atlanta, Georgia

Topic: International Comparisons

Charles M. Bruce
Partner
Butler & Binion
Washington, D.C.

Richard Gilmore
President
GIC Agricultural Group
Washington, D.C.

Bill Nourse
President
Brookemeade Hardware & Supply
Nashville, Tennessee

Erwin von Allmen
President
W.C. Smith, Inc.
Philadelphia, Pennsylvania

Other Events in Atlanta

Tour of Jimmy Carter Presidential Library

Appendix E

Authors of Commissioned Papers

Copies of these papers can be obtained from the National Technical Information Service (NTIS), Department of Commerce, after March 1987.

Steven Balkin
Department of Economics
Roosevelt University
Chicago, Illinois
Topic: Self-Employment for Low-Income People

Renee Berger and Michael Mitchell
Teamworks, Inc.
Washington, D.C.
Topic: Overseas Models of Small Business Development

Mark A. Bloomfield and Margo Thorning
American Council for Capital Formation
Washington, D.C.
Topic: Strategies for Increasing Investment in Small Business

Michael Czinkota
Center for Export-Import Studies
Georgetown University
Washington, D.C.
Topic: Encouraging U.S. Exports by Small- and Medium-Sized Firms

Robert W. Davenport
National Development Council
New York, New York
Topic: Capital Gap Facing Small Business in America

Arthur Domike
Developing Systems, Ltd.
Washington, D.C.
Topic: Promoting Small Business Exports

Richard Gilmore
GIC Agricultural Group
Washington, D.C.
Topic: Alternative Approaches to Encouraging Small Business

John Jackson
Institute for Social Research
University of Michigan
Ann Arbor, Michigan
Topic: Small Business and Job Generation

Elaine J. Malek
Fond du Lac, Wisconsin
Topic: Job Training: An Approach That Works

Ruder, Finn & Rotman
New York, New York
Topic: Small Business in America: A Survey

James Vitarello
James Vitarello Development Associates
Washington, D.C.
Topic: Capital for Small Business

THE CHALLENGE OF GLOBAL COMPETITIVENESS:

Views of America's High Growth Companies

American Business Conference

Since its inception in 1981, the American Business Conference has served as the voice of the midsize high growth sector of the economy. Comprising one hundred chief executive officers of high growth companies with revenues between $25 million and $2 billion, ABC works to create policies which promote fundamental economic growth and new opportunities for entrepreneurship.

THE CHALLENGE OF GLOBAL COMPETITIVENESS:

Views of America's High Growth Companies

PREFACE

In late autumn 1986, the American Business Conference (ABC) asked its members, the chief executives of one hundred midsize, high growth companies, to complete a survey on international competitiveness. ABC executives supplied detailed information on their companies' international performance and on their own strategies and tactics for competing in the international marketplace. Supplementary interviews were also conducted with some ABC members. This report summarizes the results of the survey and the interviews.

The survey findings reveal an astonishing record of success. Those ABC companies competing in international markets—the great majority of all ABC firms—are achieving rates of growth in international revenues often comparable to the double digit annual growth rates they enjoy in their domestic markets. This success is not restricted to any single industry. Membership in ABC is drawn from the manufacturing, service, and high technology sectors. In each sector we found evidence that American business can meet the challenge of international competition.

Encouraging as they are, the results of the survey should not be misconstrued. ABC executives are fully aware of the fragility of their international success. None are complacent about maintaining that success. Nor do they believe that their example yields easy, readily transferable lessons for industries suffering decline and job losses. If this survey is used to camouflage the grave economic problems confronting the United States, problems of which the lack of competitiveness is both a symptom and a cause, it will prove to be a counterproductive exercise.

ABC executives seek to enrich, not curtail, the current public debate on competitiveness. By offering their experience and insight, they hope to contribute to the reorientation of the policies of business and government in a direction that rewards and encourages success rather than simply protects failure. Fundamentally, America's ability to compete is an issue of economic growth and on that issue few can speak with greater practical experience than ABC members.

This report is the first in a projected series of ABC publications on aspects of the competitiveness problem. This project would not be possible without the support, interest, and cooperation of the ABC membership. In particular, we would like to recognize the work of ABC's Research and Planning Committee and its co-chairmen, Stephen Levy, Chairman and Chief Executive Officer, Bolt Beranek and Newman, Inc. and Earle Williams, President and Chief Executive Officer of BDM International, Inc.

We would also like to thank Dr. George Hatsopoulos, Chairman and President of Thermo Electron Corporation, for his continuing generosity in sharing his economic analysis of the underlying roots of the competitiveness dilemma.

Arthur Levitt, Jr., Chairman
William Lilley III, President

The American Business Conference

New York and Washington, February 1987

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“The efforts in board rooms and plants throughout the country should be toward making the best products at the lowest price so that—given a choice—consumers here and elsewhere will choose to buy them. And the efforts in Washington should be channeled toward supporting that competitive spirit, rather than trying to kid anyone into thinking that Uncle Sam can make the rest of the world go away.”

Chicago Tribune
December 28, 1986

“Trade restrictions are growth restrictions. At a time when industrialized and developing countries alike need faster growth, the industrial powers are leading in the wrong direction. The only way to win at Trade War is not with more war but with Trade Peace.”

The New York Times
January 3, 1987

“The world can hardly afford new protectionist curbs on the huge American market for foreign products. Trade expansion is vital. It creates jobs, economic growth and thus bigger markets for all countries' exports.”

The New York Times
December 8, 1986

“American performance in manufacturing is going to set the country's standard of living, as it struggles out of its gigantic trade deficit. There are only two ways to bring the trade deficit down. Either increasingly competitive American exports rise to balance the present volume of imports. Or imports will fall to meet exports, which means reduced consumption.

If American exports are going to rise to support present living standards, most of that improvement is going to have to come in the broad category of manufactured goods.”

The Washington Post
December 3, 1986

I.
FINDINGS

- ABC companies regard global competitiveness as their most important business opportunity as well as their greatest business challenge.

- ABC companies, representing all sectors of the economy, are meeting the challenge of international competition.

- ABC companies compete against their international rivals primarily on quality, value, innovation, service, and marketing.

- ABC executives believe that international competitiveness is largely a question of managerial will and skill.

- ABC executives also believe that government must supply the appropriate environment in which managerial will and skill can flourish. To that end, government must address the related problems of high capital costs and low national savings caused by large federal deficits and economic policies that reward consumption over savings.

- ABC executives identified a number of barriers to free and fair trade. Where appropriate these barriers must be challenged by government initiative. ABC executives believe that current trade law, streamlined and vigorously enforced, is sufficient. They are opposed to protectionist trade legislation.

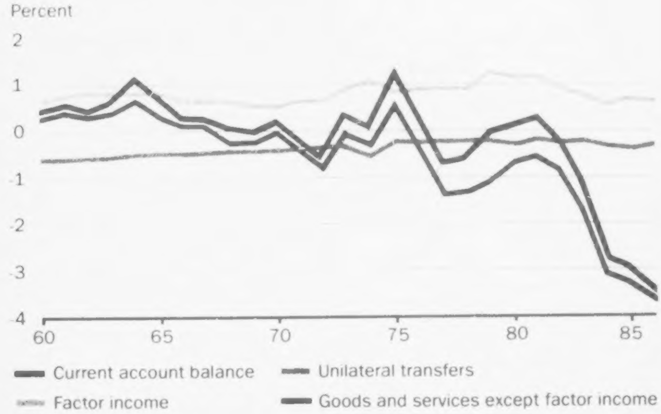
> “To raise productivity and gain real competitiveness a country must eschew protection but it also must go beyond this and learn to compete in foreign countries. . . . If foreign firms invade the American market but American firms do not invade foreign markets, foreign firms will use their secure home markets as bases from which they can pick off American firms in the American market. . . . In the world economy ahead of America, a firm that cannot compete successfully in foreign markets will not survive in the American market.”

Lester C. Thurow
The Zero Sum Solution
Simon & Schuster, 1985

> “When we are importing almost 70 percent more than we are exporting, and when the Federal Government is spending 25 percent more than its revenues, it doesn't take sophisticated economic analysis to suggest something is out of kilter. . . . To put it another way, investment has not been increasing, we are saving less and relying more on borrowing abroad, and the great growth industry (apart from Wall Street) has been importing. If all that sounds as though we are living beyond our means, well that's my conclusion, too.”

Paul A. Volcker
November 15, 1986

Components of Current Account Balance
Percent of GDP



Graph courtesy of Dr. George Hatsopoulos

II.
BACKGROUND ON INTERNATIONAL COMPETITIVENESS

The international competitiveness of the United States is not an isolated question of the relative efficiency with which American business produces and markets goods and services. Global competitiveness presupposes appropriate government macroeconomic policies, an effective educational system, a constructive relationship between labor and management, and a willingness on the part of Americans to defer a portion of their current consumption in favor of investment in the nation's future. The ability to compete internationally, while primarily a business problem, is at the same time a legitimate measure of the health of society as a whole.

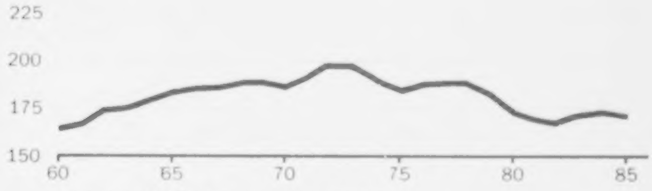
A commission appointed by President Ronald Reagan to study competitiveness developed a definition of competitiveness that suggests its importance for all Americans.

> Competitiveness is the degree to which a nation can, under free and fair market conditions, produce goods and services that meet the test of international markets while simultaneously maintaining or expanding the real incomes of its citizens.—*The Report of the President's Commission on Competitiveness* (the "Young Commission") 1985.

As this definition indicates, America cannot be considered competitive unless certain economic ends are served.

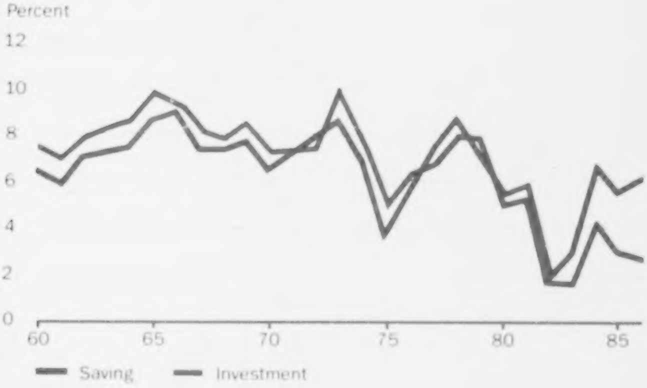
- A competitive America requires a globally competitive manufacturing sector as well as a globally competitive service sector.
- A competitive America provides an adequate standard of living for its citizens and the prospect for future improvement of that standard.

Real Average Weekly Earnings
In 1977 Dollars



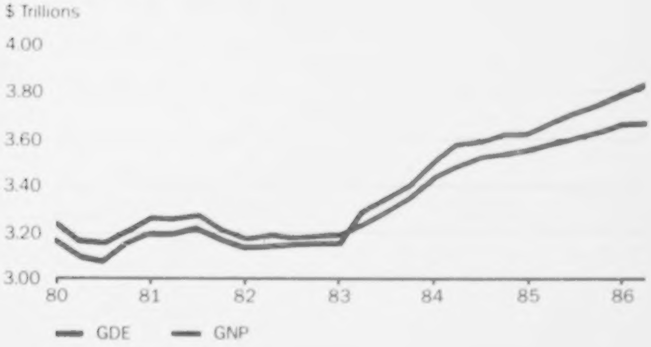
Department of Labor (Bureau of Labor Statistics)

Net National Saving and Net Investment
Percent of GDP



Dr. George Hatsopoulos

Gross National Product Vs. Gross Domestic Expenditures
In Constant 1982 Dollars



Dr. George Hatsopoulos

- A competitive America is fueled by increased earnings, not greater indebtedness.

- A competitive America, in short, promotes economic growth, the benefits of which must be accessible to those citizens and firms willing to work for success.

Judged by these standards, the United States is not competitive.

- The performance of American goods in world trade has been rapidly eroding leading to a large imbalance in American trade accounts.

- Real income per hour in the private sector has been stagnant for the past fifteen years.

- The national savings rate has proven inadequate to fund the nation's desire to consume and its need to invest.

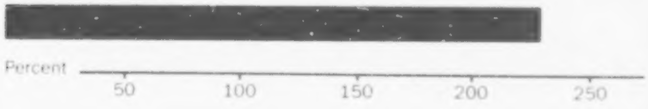
- Business decline, income stagnation, and the inadequate savings rate have led to a widening gap between what our nation spends and what it produces.

- To close the gap and maintain the standard of living, government, business, and individual Americans have increased their indebtedness.

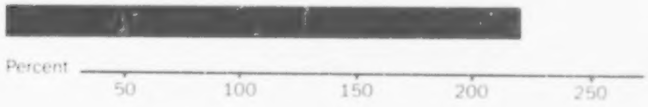
- Much of our borrowings flow from abroad. Foreign indebtedness stands at nearly 3.5 percent of GNP. The United States is the largest debtor on earth.

Existing debt must be serviced and ultimately reduced. To do so without a collapse in the standard of living, American business and, in particular, the manufacturing sector, must improve its competitive position relative to our trading partners.

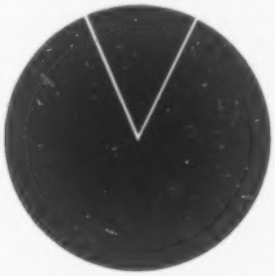
Growth of International Revenues of ABC Companies, 1980-1985



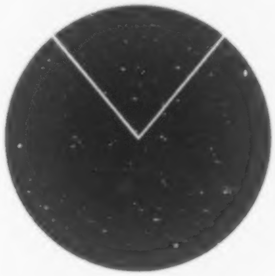
Estimated Growth of International Revenues of ABC Companies, 1986-1990



Total Revenues of ABC Companies Derived Internationally, 1982



Total Revenues of ABC Companies Derived Internationally, 1985



III.
DISCUSSION OF THE ABC SURVEY

A. ABC Companies are Internationally Competitive

Contrary to prevailing trends throughout much of American business, the ABC executives surveyed for this report have led their companies to considerable international success.

Between 1980 and 1985, ABC firms achieved an average annual growth rate in international sales of over 27 percent. For the five year period 1986-1990, ABC executives project a slightly smaller but still robust growth in international sales of over 26 percent per year.

These growth rates underscore the significance of foreign revenues as a fuel for the overall expansion of ABC firms. A 1982 McKinsey and Company survey revealed that, on average, 13.6 percent of the total revenues of ABC firms was derived internationally. Three years later, in 1985, that figure had risen to 22.1 percent. Clearly, the penetration of foreign markets has become, and will continue to be, crucial to the high growth strategies of ABC executives.

Together with the direct benefits of competing internationally, ABC executives report that participation in international markets reinforces their position at home. By seizing business from a foreign competitor in the latter's market or in third countries, ABC executives believe they can better protect their market share in the United States. Some have also found that direct exposure to foreign technologies and marketing techniques has sharpened their own already highly developed innovative and marketing skills. And, insofar as they supply other American companies with goods or services, ABC executives profit from the expansion of those companies into overseas markets.

The importance of international competitiveness

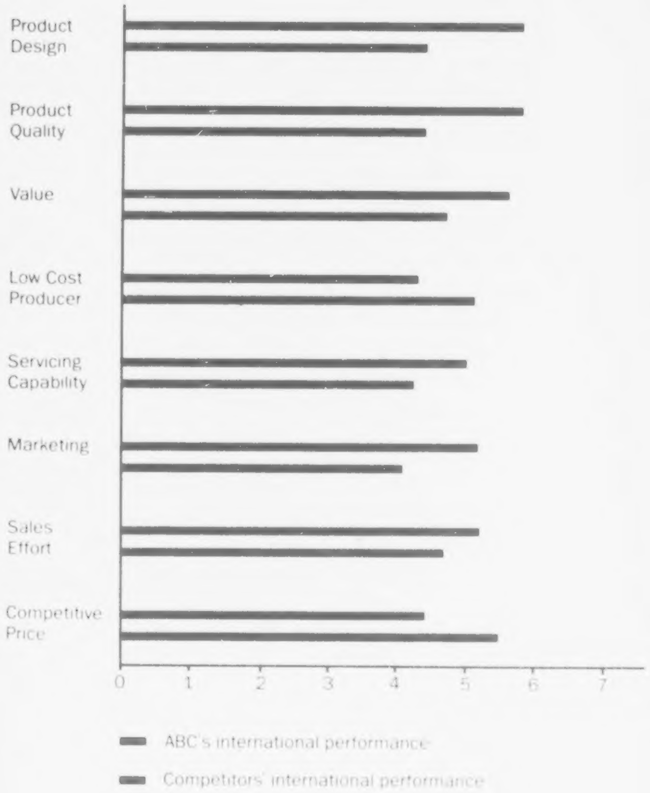
"All of our markets are worldwide—therefore our competitors are worldwide. This issue is of major strategic importance to us."
Roger Johnson, Chairman, President & C.E.O.
Western Digital Corporation

"International competition is very important as a source of revenues, diversification, and exposure to foreign technology/competition."
Charles Denny, Chairman & C.E.O.
ADC Telecommunications

"Maintenance of our successful domestic markets requires a fully-integrated and successful international presence in order to capture product innovations from abroad."
J.P. Barger, President & C.E.O.
Dynatech Corporation

"Our international competitiveness reflects our ability to attract the best people for our overseas operations and provide leadership as an industry role model."
Patrick McGovern, Chairman
International Data Group

How ABC Companies Rate Themselves Against Their Competitors



III.

B. Terms of Competition

Abraham Krasnoff, Vice Chairman and C.E.O. of the Pall Corporation, a New York-based manufacturer of filtration systems, summarized his firm's strategy for competing internationally. "Our goal is to be the low cost producer of specialty products—products with such high value that they warrant a high price. We do not sell commodities."

Allowing for differences in the products or services they sell, the great majority of ABC companies follow a similar path. A commitment to quality, to value, to innovation, and to service on the one hand, and the ability to identify—or even create—markets on the other, distinguish ABC executives.

To these qualities ABC executives bring an attitude of relentless optimism. That optimism, which is a product of self-confidence, allows them to take business risks. It grants them patience to sustain early losses in order to establish a presence in new markets. It gives them and their companies a sense of purpose. Optimism, as much as any single personal characteristic, is the catalyst for their success.

Comments regarding competitive strategies

"We compete by promoting value-added products, niche marketing, better product performance, more product variety, and by using entrepreneurial salesmen."

Roland Boreham, Chairman & C.E.O.
Baldor Electric Company

"We generally sell our products on technical merits, and on a 'total service' approach not offered by other vendors."

Stephen R. Levy, Chairman & C.E.O.
Bolt Beranek and Newman Inc.

"We distinguish our products with image-building advertising and quality workmanship/design."

W. L. Lyons Brown, Jr., Chairman & C.E.O.
Brown-Forman Corporation

"We invented both our technology and our markets."

Robert Krieble, Chairman (ret.)
Loctite Corporation

"We emphasize client service."

Larry Horner, Chairman & C.E.O.
Peat, Marwick, Mitchell & Company

"We compete internationally in the same way as we do in the United States: quality, price, and service."

T. J. Dermot Dunphy, President & C.E.O.
Sealed Air Corporation

"Technological improvements have been the critical determinant of our international sales. To overcome domestic competitors and other exporters, we have found that, in general, we must offer superior performance and value. We have also learned that exceptional reliability and long operating lives are even more important in international markets because customers are concerned with how far away they are from our production facilities. Finally, effective cost-control has proven to be very important."

George Hatsopoulos, Chairman & President
Thermo Electron Corporation

"We compete by offering/emphasizing U.S. technology as the best in the world."

Earle Williams, President & C.E.O.
BDM International, Inc.

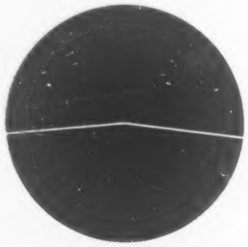
"We attack foreign competitors on their own home ground by doing the job better in all aspects."

Abraham Krasnoff, Vice Chairman & C.E.O.
Pall Corporation

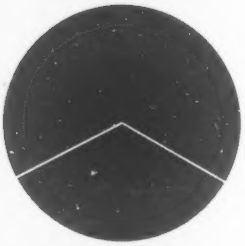
International Competitiveness: Other Business Views

Findings from a 1986 survey by Egon Zehnder International of one hundred executives from the nation's *largest* industrial and service firms:

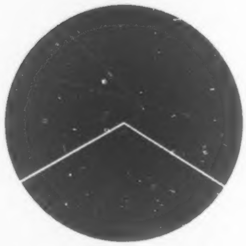
Believe foreign markets are more open than their companies assume



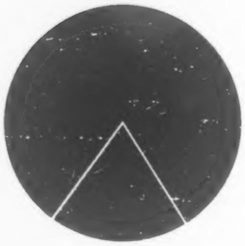
Think their colleagues are "woefully ignorant" about foreign markets



Cite management's lack of initiative as greatest barrier to overseas expansion



Oppose import quotas as way to reduce world competitive pressures on their companies



III.

C. Forms of Competition

While the terms on which ABC companies compete internationally are fixed—quality, service, innovation, and superior marketing—the form or manner in which they compete is not. Agility is the only constant denominator in the approach ABC companies adopt toward entering a foreign market. As Roland Boreham, Chairman & C.E.O. of Baldor Electric Company has said, American companies seeking to compete internationally cannot adopt a single set of tactics—they must be prepared to use "anything that works."

Nonetheless, the survey of ABC executives did reveal certain attitudes and considerations that typically influence the manner in which they compete abroad. For example, ABC executives are averse to sharing the risks or rewards of international competition. Eighty-two percent said they prefer to enter foreign markets unilaterally rather than pursue cooperative arrangements with indigenous firms. When they do undertake joint ventures, partnerships, or licensing arrangements, it is often because tariffs or non-tariff barriers such as technology transfer requirements preclude direct, economical access to target markets.

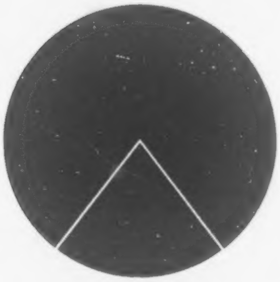
Although wary of cooperative arrangements with foreign firms, most ABC executives endorse the use of foreign nationals in positions of responsibility. The accounting firm of Arthur Andersen and Company, for example, has tapped the "huge opportunities" its senior partner, Robert Philip, sees in international markets by establishing separate operating units in over forty countries managed exclusively by local personnel trained by the company.

Other ABC executives report that a foreign sales force helps them to identify business opportunities, ease cross-cultural communication, and improve marketing strategies. ABC executives with manufacturing facilities overseas also benefit from foreign management. According to John Gilmartin, President & C.E.O. of Millipore, the harshest critics of his company's products are the managers of his Japanese plant.

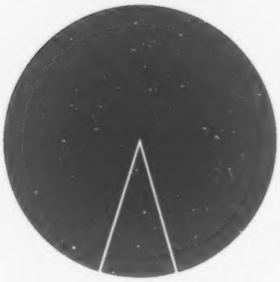
International Competitiveness: Other Business Views

Findings from a 1986 survey by the Bank of Boston of representatives of *small* business:

- Small business executives believe that product quality and aggressive marketing are chief prerequisites to successful exporting strategy.
- Small business executives primarily blame adverse macroeconomic conditions, particularly an unfavorable exchange rate, for reductions in American exports.



Oppose quota and tariff restrictions on foreign imports



Favor pursuit of multilateral trade negotiations

For them, production of an absolutely superior product is a matter of personal honor.

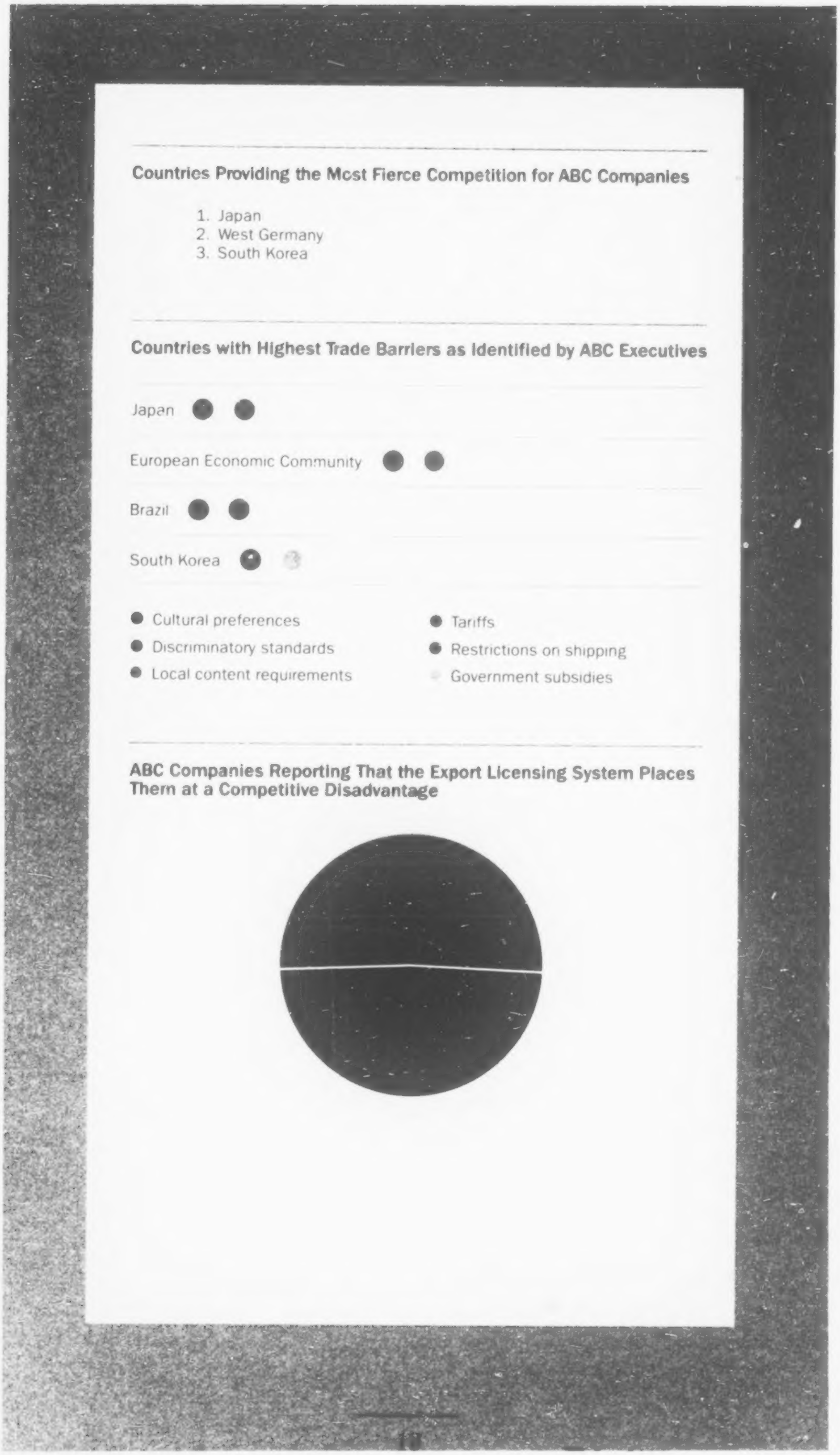
ABC executives were asked whether they had moved manufacturing facilities offshore to reduce costs within the last five years. Forty-seven percent answered affirmatively. Ireland, Mexico, Puerto Rico, and Taiwan were the most commonly named sites for new plants.

Roger Johnson, Chairman of Western Digital Corporation, offered a suggestive perspective on his decision to locate facilities in Cork, Ireland. Labor and resource costs had minor relevance. Johnson stresses instead the importance of controlling *total* costs. The main components of Western Digital's total costs are, in descending order of importance:

1. cost of market access
2. cost of capital/taxes
3. cost of customer support
4. cost of labor/manufacturing

Johnson argues that for many high growth companies the first two costs typically dictate the location of new manufacturing facilities. Unless those costs are favorable, American labor could offer its services for free and Western Digital would still move offshore. With a favorable tax rate and a net cost of capital of 3 percent in Ireland, it would be bad business not to relocate.

Roger Johnson doubts that policy makers understand these new business realities. As he sees it, the competitiveness debate in Washington assumes a manufacturing sector that is largely labor intensive. Today, competitive manufacturing depends instead upon the skillful use of capital to acquire appropriate technologies and to train employees to put those technologies to use. Accordingly, to maintain the nation's manufacturing base, government must promote economic policies that yield a favorable cost of capital, a competitive and stable rate of monetary exchange, and a tax system that encourages savings and investment.



Countries Providing the Most Fierce Competition for ABC Companies

1. Japan
2. West Germany
3. South Korea

Countries with Highest Trade Barriers as Identified by ABC Executives

Japan ● ●

European Economic Community ● ●

Brazil ● ●

South Korea ● ○

● Cultural preferences
● Discriminatory standards
● Local content requirements
● Tariffs
● Restrictions on shipping
○ Government subsidies

ABC Companies Reporting That the Export Licensing System Places Them at a Competitive Disadvantage

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III.

D. Trade Barriers

ABC executives identified a variety of tariff and non-tariff trade barriers that impede their ability to enter foreign markets. Some of these barriers can and should be lowered through governmental action. ABC executives believe that current trade laws, vigorously applied, are sufficient for the task. They oppose protectionist legislation.

1. Explanation of foreign trade barriers

Cultural preferences were the most common foreign barrier to trade identified by ABC executives. Under this category are grouped a number of manifestations of cultural chauvinism. These include the reluctance of talented foreign technicians and sales people to join American-owned subsidiaries, the tendency of governments to rely upon local suppliers, and the unwillingness of consumers—both individuals and firms—to buy American products and services. Japan and the members of the European Economic Community (EEC) were the countries most often associated with the cultural preferences barrier. ABC executives specifically singled out the EEC for domestic content requirements.

Tariffs constituted the second most commonly cited trade barrier. Brazil is particularly notorious for its prohibitively high tariffs. ABC executives also fault Korea and Japan on this score.

Discriminatory regulatory standards, a problem associated almost exclusively with Japan, was the third most commonly cited trade barrier. This category encompasses a variety of unpredictable, prejudicial, or unevenly applied regulatory policies. One example offered by an ABC executive is Japan's lengthy patent process. It effectively blocks the introduction of innovative products until local firms have had time to catch up. Other executives cited instances in which their products were rejected by Japanese authorities for seemingly irrelevant reasons such as "improper" packaging.

Additional foreign trade barriers identified by ABC

“Exports from the United States and re-exports from approved countries are regulated by a system of licenses. The regulations are massive—covering some 600 pages—and, according to the panel, are not generally perceived as rational, credible, and predictable by many nations and businesses. The panel estimated that 40 percent—about $62 billion—of all U.S. exports of nonmilitary manufactured goods in 1985 were shipped under a license requiring prior approval. The process is often slow, and 52 percent of U.S. exporters surveyed as part of the study reported lost sales primarily as a consequence of licensing requirements. The problems seem to be more pronounced for small business firms, the panel said.”

Press Release, January 14, 1987
summarizing the findings of the
National Academy of Science's
Balancing the National Interest:
U.S. National Security Export Controls
and Global Economic Competition

executives include: data flow restrictions, discriminatory tax policies, prohibitions against the repatriation of capital, and technology transfer requirements.

2. Export licensing

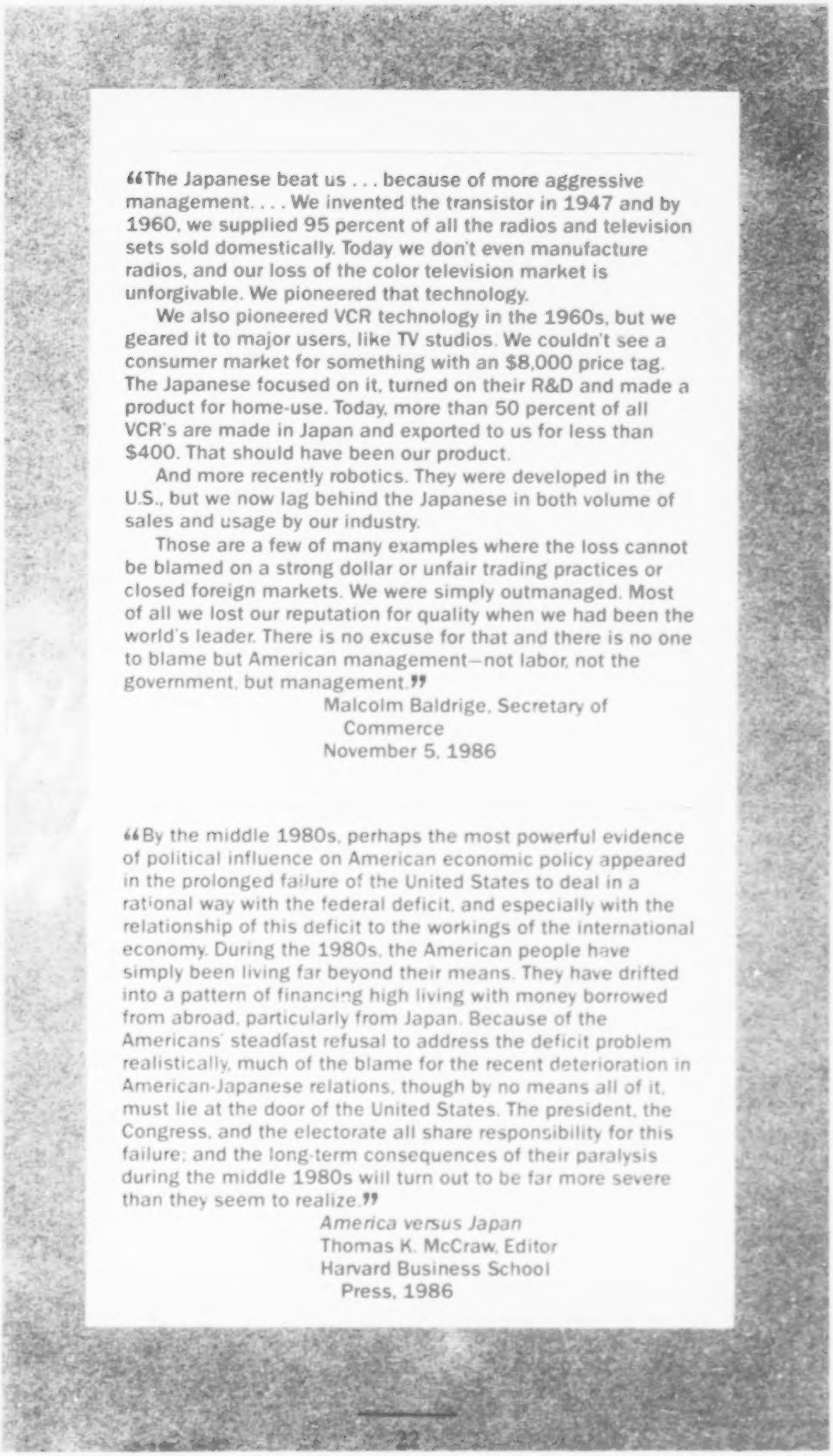
Not all trade barriers are of foreign origin. The export licensing system, which is designed to prevent the export of strategically sensitive technology and is administered by the American government, has placed over half of the ABC companies at an international competitive disadvantage.

ABC executives describe the process for obtaining an export license as unnecessarily cumbersome, and marked by squabbling between the Departments of Commerce and Defense. The delay can cost sales since other nations administer their export licensing programs far more efficiently. For example, it takes the United States government an average of 145 days to issue an export license for a Cray Research supercomputer. The government of Japan licenses the export of Japanese supercomputers in thirty days.

The failure of the United States to develop an export licensing system that takes due regard of the nation's strategic interest without unnecessarily impinging on American export sales is in itself a national security issue. As John Rollwagen, Chairman of Cray Research, Inc., notes, "When U.S. high technology manufacturers lose their market share, they lose precious revenue to continue their research and development. Without that revenue for R&D, U.S. corporations will lose their preeminent standing and the country will become dependent on foreign manufacturers for critical technologies."

3. The special case of Japan

By a two-to-one margin, ABC executives identified Japanese companies as their most fierce competitors. By a similar margin, they named the Japanese market as the most resistant to entry. Both observations are part of the same phenomenon:



“The Japanese beat us . . . because of more aggressive management. . . . We invented the transistor in 1947 and by 1960, we supplied 95 percent of all the radios and television sets sold domestically. Today we don't even manufacture radios, and our loss of the color television market is unforgivable. We pioneered that technology.

We also pioneered VCR technology in the 1960s, but we geared it to major users, like TV studios. We couldn't see a consumer market for something with an $8,000 price tag. The Japanese focused on it, turned on their R&D and made a product for home-use. Today, more than 50 percent of all VCR's are made in Japan and exported to us for less than $400. That should have been our product.

And more recently robotics. They were developed in the U.S., but we now lag behind the Japanese in both volume of sales and usage by our industry.

Those are a few of many examples where the loss cannot be blamed on a strong dollar or unfair trading practices or closed foreign markets. We were simply outmanaged. Most of all we lost our reputation for quality when we had been the world's leader. There is no excuse for that and there is no one to blame but American management—not labor, not the government, but management.”

Malcolm Baldrige, Secretary of
Commerce
November 5, 1986

“By the middle 1980s, perhaps the most powerful evidence of political influence on American economic policy appeared in the prolonged failure of the United States to deal in a rational way with the federal deficit, and especially with the relationship of this deficit to the workings of the international economy. During the 1980s, the American people have simply been living far beyond their means. They have drifted into a pattern of financing high living with money borrowed from abroad, particularly from Japan. Because of the Americans' steadfast refusal to address the deficit problem realistically, much of the blame for the recent deterioration in American-Japanese relations, though by no means all of it, must lie at the door of the United States. The president, the Congress, and the electorate all share responsibility for this failure; and the long-term consequences of their paralysis during the middle 1980s will turn out to be far more severe than they seem to realize.”

America versus Japan
Thomas K. McCraw, Editor
Harvard Business School
Press, 1986

twentieth century Japanese mercantilism. In order to underwrite their international ventures, Japanese firms rely upon their domination of a secure home market.

As ABC executives noted, American penetration of the Japanese market is vital to meeting Japan's competitive challenge around the world. At issue is how best to open the Japanese market to American business. An answer may lie in an examination of the trade barriers ABC executives attribute to the Japanese. The barrier they cite overwhelmingly is cultural preference. Alteration of cultural habits cannot usually be accomplished through government action. Overcoming cultural chauvinism is essentially a function of the will and skill of American managers. While the growth rates of ABC firms may not be attainable by other, larger companies, the managerial attitudes that made such rates possible are. Unless American business as a whole makes the necessary investment in quality, service, innovation, and strategic marketing, it will never become fully competitive in Japan.

This is not to argue that the American government has no role to play in opening the Japanese market. Some Japanese trade barriers can only be eliminated or, at least, mitigated, through diplomatic pressures. Further, having seen some of the brightest American growth companies of a few years ago—such as those in the semiconductor industry—succumb to Japanese targeting, ABC executives are not prepared to have the government abandon the field of battle.

Nevertheless, ABC executives would argue that government can best help American business penetrate the Japanese market by reducing the federal debt, establishing a sound monetary and tax policy, and encouraging intelligent regulatory and educational reforms. Protectionism, on the other hand, is of no help at all. In the end, government must place the central responsibility for American competitiveness in Japan and elsewhere upon the shoulders of American business where, in our society, it belongs.

“When the Senate Finance Committee opened its hearings on the trade deficit, it confronted an unpleasant reality. The American trade deficit doesn't really depend on Japanese commercial tactics or the low wages in Korean factories. It depends on the way Americans are running their own economy. As long as they run it in a manner that depends on a heavy flow of borrowed money from abroad, the country will have large trade deficits.

A lot of people in Congress think that if the trade deficit could somehow be forced down by law, the result would be more jobs here in the United States. That's flatly and dangerously wrong. If the United States could cut off all imports from Japan tomorrow morning by a magical spell one of two things would happen. Either the deficit would remain the same, with the imports coming in from other countries, or the United States would slide into a deep recession. To try to reduce the trade deficit without first changing the internal balance of the economy—above all, by getting the federal budget deficit down—would be both futile and harmful to the country's welfare.”

The Washington Post
January 19, 1987

IV.
FINAL POINTS

This report offers no specific policy recommendations. Instead, forthcoming ABC reports will provide extended discussions of the policy issues raised by the survey, in particular the need to create an appropriate macroeconomic environment for international competitiveness.

At the beginning of this report, America's international competitiveness was said to be deficient. This problem cannot be solved by avoiding it. To retreat from foreign markets because they are difficult to enter, to retreat from the principles of free and fair trade, to retreat from the discipline of competition, is to retreat from our future. Unless we can affirm the values of quality, service, and innovation, we will find ourselves backing into the next decade and into the next century. Other nations will not wait for us to get turned around.

"Analog Devices is running scared. We don't feel at all comfortable about our competitive posture, and we feel the pressure to change our business strategy in order to be successful in the future. In the broadest terms we and other American corporations have depended on product differentiation to extract premium prices from the marketplace. This differentiation could be derived from innovation, quality, and service. Looking to the future, we cannot sidestep the issue of costs and competitive pricing in the international market. The posture of standing aloof from nitty-gritty competition based on a technology gap or other differentiating factors as important as they are and will continue to be is no substitute for aggressive management of productivity and costs. It is not an either/or game; we must not only be leaders in innovation but in cost as well. In this respect we will need all the help we can get, including a competitive cost of capital and the support of a superior educational system."

Ray Stata, Chairman & President
Analog Devices

APPENDIX A

ABC Competitiveness Survey

I. GENERAL COMPETITIVENESS

1. How important to your company is the international competitiveness of the U.S.?
2. Please approximate what percentage of your 1985 sales were derived internationally. ____________________
3. Please approximate the percent sales growth of your international business 1980-1985. ____________________
4. Please approximate the projected percent sales growth of your international business 1986-1990. ____________________
5. For the international market, would you characterize your 1990 projection as
   a. Aggressive b. Reasonable c. Conservative
6. Based on your knowledge and experience, do you feel the firm will likely
   a. Exceed 1990 international projections,
   b. Meet 1990 international projections, or
   c. Not meet 1990 international projections?
7. In general, how do profits on foreign sales contrast to profits on domestic sales?
   ________ greater
   ________ same
   ________ less
8. From what three countries is foreign competition most fierce?

   ____________ ____________ ____________
   Most competitive 2nd Most competitive 3rd Most competitive
9. If you have faced significant competition from foreign companies, how have you been able to counter this competition?
10. Thinking of the potential of the international market as you see it, how well do you feel your firm's 1985 performance in the international market has met its potential? Would you say performance
    a. Exceeded potential b. Met potential c. Fell below potential
11. In 1985, did international markets exist for which you saw great potential for your firm, but the firm either did not compete or competed less effectively than desired?
    a. YES b. NO

11a. If you answered "Yes" to question 11, please explain why you feel your firm's potential in international markets was not met.

12. Do you have an international marketing force?
    a. YES ____________ b. NO
    (# OF PEOPLE)
13. What are the worst tariff and non tariff barriers with which your company must contend? Feel free to include, if relevant, cultural buying preferences, foreign government incentives or the need to establish a plant in a foreign country.
14. Please describe how trade barriers have affected your company.
15. Do you think trade barriers most adversely affect
    a. New products, or b. Existing products
16. Have you moved any production facilities offshore to cut costs in the last five years?
    a. YES b. NO If "yes," where? ____________________

17. Do you feel the need to obtain an export license has put your firm at a competitive disadvantage at times?

a. YES—SERIOUSLY b. YES—BUT NOT SERIOUSLY c. NO

18. FACTORS IMPORTANT TO INTERNATIONAL COMPETITION
Sections A and B ask you to rate each factor, on a scale of 1 to 7, to compare your firm to those companies (both domestic and foreign) which your firm competes against in INTERNATIONAL markets.

		A. YOUR INTERNATIONAL PERFORMANCE							B. COMPETITORS' INTERNATIONAL PERFORMANCE						
		POOR						EXCELLENT	POOR						EXCELLENT
a.	Product design	1	2	3	4	5	6	7	1	2	3	4	5	6	7
b.	Product quality	1	2	3	4	5	6	7	1	2	3	4	5	6	7
c.	Value	1	2	3	4	5	6	7	1	2	3	4	5	6	7
d.	Low cost producer	1	2	3	4	5	6	7	1	2	3	4	5	6	7
e.	Distribution channels	1	2	3	4	5	6	7	1	2	3	4	5	6	7
f.	Servicing capability	1	2	3	4	5	6	7	1	2	3	4	5	6	7
g.	Marketing	1	2	3	4	5	6	7	1	2	3	4	5	6	7
h.	Sales effort	1	2	3	4	5	6	7	1	2	3	4	5	6	7
i.	Competitive price	1	2	3	4	5	6	7	1	2	3	4	5	6	7
j.	Joint ventures	1	2	3	4	5	6	7	1	2	3	4	5	6	7
k.	High quality management	1	2	3	4	5	6	7	1	2	3	4	5	6	7
l.	Use of American managers	1	2	3	4	5	6	7	1	2	3	4	5	6	7
m.	Use of foreign managers	1	2	3	4	5	6	7	1	2	3	4	5	6	7

19. Which of the following two statements best describe your firm's strategy for competing in international markets?

_______ a. We prefer to develop cooperative arrangements with other firms who are already successful in the market we want to penetrate.

_______ b. We prefer to choose markets and products with which the firm can compete directly against other firms in the target markets.

20. Which of these two statements best describes how your firm positions its products to compete in international markets?

_______ a. We develop or enhance products so they are customized for the target market.

_______ b. We seek to develop products with universally acceptable features.

II. FOREIGN SUBSIDIARIES—OPERATING FACILITIES AND SALES OFFICES

Check below the appropriate international areas where you have operating and/or sales offices.

	1984	
	Oper. Facil.	Sales Offices
North America	_______	_______
South America	_______	_______
Western Europe	_______	_______
Eastern Europe	_______	_______
Middle East	_______	_______
Asia	_______	_______
Japan	_______	_______
Korea	_______	_______
Oceania	_______	_______
Africa	_______	_______

III. EXPORTS

Please list your three most important product categories in terms of revenues.

APPENDIX B

American Business Conference Members

As of December 1986

COMPANY	EXECUTIVE
Industrial	
Baldor Electric	Roland S. Boreham, Jr.
Brown-Forman	W.L. Lyons Brown, Jr.
Clabir Corporation	Henry D. Clarke, Jr.
A.T. Cross	Bradford R. Boss
Damson Oil Corporation	Barrie M. Damson
Devon Group	Marne Obernauer, Jr.
Endevco, Inc.	James W. Bryant
Farley Industries	William F. Farley
Goulds Pumps, Inc.	Stephen V. Ardia
Harvey Hubbell, Inc.	Fred R. Dusto
Hasbro Inc.	Stephen D. Hassenfeld
Herman Miller, Inc.	Max O. DePree
Knoll International	Marshall Cogan
Loctite Corporation	Kenneth W. Butterworth
Masco Corporation	Richard A. Manoogian
Mitchell Energy & Development	George P. Mitchell
Mosbacher Energy Corporation	Robert A. Mosbacher
Petro-Lewis Corporation	Jerome A. Lewis
Ply*Gem Industries	Jeffrey S. Silverman
Sealed Air Corporation	T.J. Dermot Dunphy
SnyderGeneral Corporation	Richard W. Snyder
Teleflex Inc.	Lennox K. Black
Thomas & Betts Corporation	J. David Parkinson
Unifi, Inc.	G. Allen Mebane
The Valspar Corporation	C. Angus Wurtele
The Yankee Companies	Graham E. Jones
Industrial High Tech	
Adams-Russell Company, Inc.	John J. Lynch
ADC Telecommunications, Inc.	Charles M. Denny, Jr.
Analog Devices, Inc.	Ray Stata
Augat, Inc.	Roger D. Wellington
Bolt Beranek & Newman Inc.	Stephen R. Levy
Bourns, Inc.	Albert R. Snider
Burndy Corporation	David Dibner
Cray Research Inc.	John A. Rollwagen
DBA Systems, Inc.	Howard N. Hebert
Dynatech Corporation	J.P. Barger
Genentech, Inc.	Robert A. Swanson
Liebert Corporation	Larry L. Liebert
Millipore Corporation	John A. Gilmartin
Pall Corporation	Abraham Krasnoff
Rogerson Aircraft Corporation	Michael J. Rogerson
Tech-Sym Corporation	Wendell W. Gamel
Teradyne, Inc.	Alexander V. d'Arbeloff
Thermo Electron Corporation	George N. Hatsopoulos
Western Digital Corporation	Roger W. Johnson
Wyle Laboratories	Stanley Wainer
Xidex Corporation	Lester L. Colbert, Jr.

PRODUCT/SERVICE	LOCATION
electric motors	Fort Smith, AK
wines and spirits, consumer goods	Louisville, KY
consumer and defense products	Greenwich, CT
writing instruments	Lincoln, RI
oil and gas	New York, NY
graphic arts	New York, NY
natural gas	Dallas, TX
diversified manufacturing	Chicago, IL
centrifugal pumps	Seneca Falls, NY
electrical products	Orange, CT
toys	Pawtucket, RI
furniture	Zeeland, MI
furniture	New York, NY
adhesives and sealants	Newington, CT
diversified manufacturing	Taylor, MI
oil and gas	The Woodlands, TX
oil and gas	Houston, TX
oil and gas	Denver, CO
wood products and filter media	New York, NY
protective packaging	Saddle Brook, NJ
heating, air conditioning and refrigeration	Dallas, TX
applications engineering products	Limerick, PA
electrical connectors	Raritan, NJ
textured polyester	Greensboro, NC
paint and related coatings	Minneapolis, MN
oil, gas, and financial services	Cohasset, MA
signal processing equipment	Waltham, MA
telecommunications components	Minneapolis, MN
integrated circuits	Norwood, MA
electro-mechanical components	Mansfield, MA
R&D products and services	Cambridge, MA
military and scientific equipment	Riverside, CA
electronic connectors and electrical power components	Norwalk, CT
supercomputers	Minneapolis, MN
defense, graphics, sensing and diagnostic systems	Melbourne, FL
data communications and test and medical instruments	Burlington, MA
medical products	San Francisco, CA
computer support systems	Columbus, OH
fluid purification products	Bedford, MA
filtration equipment	Glen Cove, NY
advanced aircraft	Irvine, CA
defense electronics	Houston, TX
test equipment	Boston, MA
instruments and co-generation systems	Waltham, MA
computer subsystems	Irvine, CA
electronic components and systems	El Segundo, CA
floppy disks and other data storage products and services	Mountain View, CA

COMPANY	EXECUTIVE
Services	
Arthur Andersen & Company	Robert W. Philip, Jr.
Automatic Data Processing, Inc.	Josh S. Weston
BDM International, Inc.	Earle C. Williams
Bergen Brunswig Corporation	Emil P. Martini, Jr.
Beverly Enterprises	Robert W. Van Tuyle
Bill Communications	John W. Hartman
California Plant Protection	Thomas W. Wathen
Care Enterprises	Lee Bangerter
Charter Medical Corporation	William A. Fickling, Jr.
CCA Investment Corporation	James A. Maser
Comdisco, Inc.	Kenneth N. Pontikes
Community Psychiatric Centers	Robert L. Green
Computer Language Research Inc.	Stephen T. Winn
Comp-U-Card International, Inc.	Walter A. Forbes
Cosmopolitan Care Corporation	Ronald Berman
Cullinet Software	John C. Cullinane
Dunkin' Donuts, Inc.	Robert M. Rosenberg
Electro Rent Corporation	Daniel Greenberg
The Forum Group, Inc.	O.U. Mutz
Grey Advertising, Inc.	Edward H. Meyer
Harte-Hanks Communications, Inc.	Bob Marbut
Heritage Communications, Inc.	James M. Hoak
Horn & Hardart Company	Barry M. Florescue
Intermark, Inc.	Charles R. Scott
International Data Group	Patrick J. McGovern
Josephson International, Inc.	Marvin Josephson
Korn/Ferry International	Lester B. Korn
Levitz Furniture Corporation	Robert M. Elliot
Marketing Corporation of America	James R. McManus
Meredith Corporation	Robert A. Burnett
Pandick Inc.	Edward G. Green
Peat, Marwick, Mitchell & Company	Larry D. Horner
Rykoff-Sexton, Inc.	Roger W. Coleman
Safeguard Business Systems, Inc.	Vincent G. Bell, Jr.
Safety Kleen Corporation	Russell Gwillim
SMS	R. James Macaleer
Standard Brands Paint Company	Stuart D. Buchalter
URS Corporation	Arthur H. Stromberg
Wherehouse Entertainment, Inc.	Louis A. Kwiker
Financial and Real Estate Services	
American First Corporation	J. David Markley
Birtcher	Arthur B. Birtcher
Chilton Corporation	J.E.R. Chilton III
Donaldson, Lufkin & Jenrette, Inc.	John S. Chalsty
Drexel Burnham Lambert, Inc.	Robert E. Linton
Fairfield Communities, Inc.	C. Randolph Warner, Jr.
The Foothill Group	Don L. Gevirtz
Great American First Savings Bank	Gordon C. Luce
Heizer Corporation	Edgar F. Heizer, Jr.
Integrated Resources	Arthur H. Goldberg
Jack Resnick & Sons, Inc.	Burt P. Resnick
Landmark Bancshares Corporation	S. Lee Kling
NVHomes	Dwight C. Schar
New Plan Realty Trust	William Newman

PRODUCT/SERVICE	LOCATION
accounting	Dallas, TX
computer processing	Roseland, NJ
defense related technical/professional services	McLean, VA
distribution of health care products and tapes	Orange, CA
nursing homes and care facilities	Pasadena, CA
publishing	New York, NY
security guards	Van Nuys, CA
nursing homes	Laguna Hills, CA
medical treatment services	Macon, GA
club management	Dallas, TX
remarketing of used computer equipment	Rosemont, IL
psychiatric hospitals	San Francisco, CA
tax processing	Carrollton, TX
electronic shopping	New York, NY
temporary health care personnel	Stamford, CT
computer software	Westwood, MA
coffee and doughnut shops	Randolph, MA
electronic equipment leasing	Santa Monica, CA
retirement homes	Indianapolis, IN
advertising	New York, NY
communications	San Antonio, TX
cable television	Des Moines, IA
fast food and mail order marketing	New York, NY
diversified retailer	La Jolla, CA
publisher of computer magazines	Framingham, MA
entertainment	New York, NY
executive search firm	Los Angeles, CA
furniture retailer	Boca Raton, FL
consumer marketing services	Westport, CT
publishing and broadcasting	Des Moines, IA
financial printing	New York, NY
accounting	New York, NY
food distributor	Los Angeles, CA
management information systems	Ft. Washington, PA
parts cleaner services	Elgin, IL
medical information systems	Malvern, PA
retailer of home decorating products	Torrance, CA
engineering and construction	San Mateo, CA
video cassete rental	Torrance, CA
insurance and financial services	Oklahoma City, OK
commercial real estate	Santa Ana, CA
credit reporting	Dallas, TX
financial services	New York, NY
financial services	New York, NY
real estate	Little Rock, AK
commercial finance	Los Angeles, CA
savings bank	San Diego, CA
venture capital	Chicago, IL
financial services	New York, NY
real estate, construction and management	New York, NY
multibank holding company	St. Louis, MO
real estate and construction	McLean, VA
real estate	New York, NY

PREPARED STATEMENT OF GORDON O.F. JOHNSON, PRESIDENT, JOHNSON ASSOCIATES

Mr. Chairman and Members of the Committee:

My name is Gordon Johnson. I am President of Johnson Associates, which is my own small business consulting firm, and former President and Chief Executive Officer of LogEtronics Inc., in Springfield, Virginia, a capital equipment manufacturing company which I helped found in 1955. Over a thirty year period, we grew to approximately $30,000,000 in sales and 350 employees and competed successfully against companies such as Eastman Kodak and Dupont.

The principal products of LogEtronics are photographic and computer imaging equipment for the graphic arts industry, as well as for aerial photography and medical radiography. We have users of our equipment in over 90 countries around the world and received the President's "E" Award for Export Expansion in 1979. I also serve currently as Deputy Director of the Center for Privatization, providing consulting services to the Agency for International Development in assisting developing countries privatize their state owned enterprises.

My remarks to you here today are based on my 30 years experience in building LogEtronics to its position today as a leading world supplier of prepress equipment for the printing and publishing industry. I have been actively involved in the issue of how to increase small business exports in a variety of capacities over the past 10 years, including the Advisory Committee of the Export Import Bank, the Commerce Department/USTR Industry Sector Advisory Committee for Small and Minority Business, and the U.S. Chamber of Commerce Small Business Council and Export Policy Task Force. It was my special privilege to serve as a delegate from Virginia to the White House Conference on Small Business in 1986, and to help draft Recommendation #35, which deals with ways to increase small business exports.

THE BASIC ISSUE:

I believe that in dealing with international trade issues, we are dealing with the survival of this nation as a strong viable force among free world nations. We are living on borrowed time, financed by borrowed money. We are a debtor nation for the first time since 1914, but this time we are borrowing to support consumption instead of increased production capacity. Certainly we should be grateful that foreign investors are willing to buy our bonds and invest in our country, but we are being very naive if we think this method of financing our deficit can continue indefinitely--it has already continued longer than many of us ever thought possible. Sooner or later our excess imports must be paid for by an excess of exports.

Where will the needed increase in exports come from? Obviously the decrease in the value of the dollar in relation to the currencies of some of our major competitors will be a substantial help across the board for all present exporters, but at the same time we must also recognize that the lower dollar will generate increased pressure for various forms of non-tariff protection in overseas markets. Certainly we will not win back easily and quickly the markets lost when the strong dollar made it difficult to compete effectively in foreign markets.

SMALL BUSINESS - PART OF THE SOLUTION:

One important source of increased exports is small business. Some small businesses are already active in foreign markets,but there are many more which are not. Some are real marketeers, while others are simply order-takers. After all there may be an export imperative for the nation, but there is certainly no export imperative for most small U.S. businesses. There is generally plenty of opportunity to grow with less risk, and more profitably, by expanding small business marketing efforts in known U.S. domestic markets.

If the nation really wants more exports by small business, it will have to face the fact that the incentives to export must somehow be increased. Small business owners are not dumb, lazy or ignorant when it comes to international trade. They know that export markets are more complex, and involve more hassle and more risk than their domestic markets. The obstacles are much larger in proportion to their total business, and the personal stakes far higher, than they are in bigger businesses. Small businesses were the hardest hit by, and least able to cope with, the strong dollar. Small businesses are also the hardest hit by non-tariff barriers.

GOVERNMENT HAS BEEN TRYING:

It isn't that government hasn't been trying! Over the past 8 or 10 years, we have seen innumerable seminars on how to export, instruction booklets on exporting, invitations to join foreign trade missions, international trade fair arrangements, foreign market data reports, prospective buyer leads, foreign sales agent lists, export financing assistance, credit guaranty programs, etc. etc. The Export Import Bank has certainly improved its ability in recent months to serve small business. And then there are the Export Trading Companies out there looking for clients to serve, trying to do what Government has not been able to do effectively.

In short, there are a number of players on the scene anxious to help small business do more exporting. There are many wares on the shelf which could help small business, and more are being developed or proposed every day. The real question which needs to be answered first, however, is how to get the small business owner's attention, how to get him into the store in the first place to want to try out the wares. Until the owner really decides positively to commit to an increased priority for exports, nothing really different will happen within the company. Foreign travel will take place when, as and if there is slack time to do it; 50-cycle machines for foreign customers will continue to be worked on only after we are caught up on production of 60-cycle machines for domestic customers; literature will get translated into Spanish or French when there is room in the budget to be able to afford it.

How indeed do we get small business' attention and priority on exports to meet the nation's imperative need to reduce the trade deficit?

WE NEED MEANINGFUL AND MARKETABLE INCENTIVES:

In order to get the attention of small business owner-presidents, there is a real need to create meaningful and marketable financial incentives.

One small example already underway is the "Shared Foreign Sales Corporation" being actively promoted by the State of Delaware under the headline: "15% Federal Tax Exemption Possible". The IRS may not appreciate this kind of marketing, but something along those lines is absolutely essential to get attention.

The White House Conference on Small Business went even further with respect to the FSC, and recommended a greater reduction in tax for the "Small FSC" as compared to the regular FSC, together with simplification of the transfer pricing formula so the small business could indeed calculate in advance of a sale what the tax benefit would be. (European competitors get that now with their refunds on VAT taxes at the time of sale.)

One of the genuinely new ideas to come out of the 1986 White House Conference on Small Business, was the proposal to establish an "Export SBIR" program modelled on the process developed under the highly successful Small Business Innovation and Research (SBIR) program to bring the talents and creativity of small business to bear on the nation's R & D programs. The SBIR program has been very effective in bringing small business and government together to solve problems with a minimum of paper work and bureaucratic procedures. Why not try this same approach to solve some of our nation's export problems?

The basic principle underlying the SBIR program is that government should define critical problems, and then seek out and listen to innovative solutions proposed by small business. The best of those proposals would then receive a grant award of a fixed sum of money to do a feasibility study. Instead of writing voluminous specifications which were then frozen and put out to the lowest bidder, the SBIR approach was to seek out the maximum performance for a pre-announced fixed price. Instead of the government deciding what should be in the specifications, it asked the small business bidders to spell out what they thought should be in the specifications, and then selected only the very best proposals.

Why not apply this same basic approach to small business exports?

Instead of thinking up all the possible services which might be useful for a small business going into new overseas markets, why not ask the small business what it thinks it really needs to do to increase its exports? (We should note in passing that these services are often hard to find out about, as perhaps you read recently in the Wall Street Journal article about the Japanese translation of a U.S. Census Bureau study of consumer buying habits and trends in China which was widely distributed throughout the Japanese business community long before anyone in the U.S. was really aware of its existence. --WSJ 11/19/86)

SMALL BUSINESS EXPORT INNOVATION AWARDS:

A program soliciting Export Increase Proposals from small businesses, which might be called the Small Business Export Innovation Award program, operating along the same general lines as the SBIR program for R&D, would have some very positive characteristics:

(1) It would not involve new appropriations, but instead would be funded as a set-aside from moneys already appropriated for international trade development and servicing.

(2) It would serve as a marketing vehicle for private sector export service firms to sell their services to eligible small businesses. The same would also apply for State export development offices and local universities with international trade departments, who could offer their help and assistance to small businesses in developing winning proposals. Commerce Department Foreign Commercial Officers would also find an Export Innovation Awards program a useful tool to get the attention of small business exporters.

(3) If the program is effectively marketed, and if it follows the same pattern as the SBIR program, one could expect some 8 to 10 Export Increase Proposals for every actual winner -- ie, 8 to 10 firms would have started thinking seriously about how to increase exports, for every one that actually wins an award.

(4) A program which would provide 100 to 200 awards of $25,000 each, with a requirement for an equal matching amount of new funds for export promotion by the award winners would create meaningful incentives among small businesses throughout the nation if it is properly promoted.

SUMMARY:

Our nation must reduce its deficit in international trade -- and do it soon! The best solution is to export more, rather than importing less. Programs to increase exports generate increased jobs in our most competitive "sunshine" industries and at the same time increase tax revenues to help reduce the budget deficit.

Small business represents a significant potential for increased exports, but will require meaningful and marketable financial incentives before it will divert more resources away from its present priority domestic markets.

To get the customer into the store, the first thing you have to do is get his attention! One way to get attention is to improve the tax benefits for the Small Foreign Sales Corporation to be more equivalent to the VAT tax refunds to European competitors. Another way to get attention would be to establish a Small Business Export Innovation awards program modelled after the approach used in the highly successful Small Business Innovation and Research program. Both of these recommendations were named among the final 60 recommendations of the 1986 White House Conference on Small Business.

The Export Innovation Award program could be funded without any new appropriated funds by establishing a set-aside within present international trade development funds and would provide an extremely effective marketing tool for the many private and public export service groups looking for ways to help small businesses do more exporting.

If we are indeed serious about encouraging more small businesses to increase their emphasis on exporting, it won't come about simply by standing on rooftops and shouting at them. It will take meaningful financial incentives. Most of them know a great deal more about how to run their business and where to invest their precious time and resources than any outsiders ever will!

PREPARED STATEMENT OF WILLIAM LILLEY III, PRESIDENT, AMERICAN BUSINESS CONFERENCE [ABC]

Mr. Chairman and members of the Committee, I am pleased to testify today on behalf of the American Business Conference (ABC) on the issue of America's international competitiveness. Our members applaud you for holding this hearing. The Small Business Committee brings to the competitiveness debate an important perspective and set of concerns that deserve the nation's attention.

The American Business Conference is a coalition of one hundred chief executives of midsize, high growth companies. At minimum, ABC companies must demonstrate an annual revenue growth at a level three times the growth of the economy plus inflation. In fact, the average ABC company grows at a far higher rate -- about 35 percent per year. The average annual revenues of ABC companies is $370 million.

ABC companies are not representative of small business as the latter is typically construed. Yet the midsize firms I represent share with smaller companies certain functional and attitudinal affinities.

These affinities, especially as they relate to international competitiveness, explain my presence here today.

Like their smaller counterparts, ABC companies are entrepreneurial in spirit. ABC executives typically founded their companies, or rose to prominence within them, based either on their marketing expertise or their ability to create new products and services. Not surprisingly, ABC firms depend upon a continuing stream of innovation and a capacity to discern lucrative new markets for those innovations.

ABC firms are creating new jobs at a median rate of 13.5 percent annually. In this way, too, they mirror the dynamism of the small business sector which accounts for an estimated 80 percent of the jobs created in the United States each year. The extraordinary contribution of entrepreneurial firms to the American economy belies the expectations of social observers of a few years ago who linked the nation's future to the fortunes of large corporations controlled by professional managers. Entrepreneurialism is far from obsolete.

Yet, despite their vigor, small and midsize companies have not been represented adequately in the current debate on competitiveness. In part, this is a result of the nature of such firms. ABC companies, for example, typically do not have Washington offices, batteries of lobbyists, or public relations staffs. ABC executives are themselves deeply involved in operating their businesses, leaving little time for visits to Washington. Except in a forum such as this one, which specifically solicits the views of smaller companies, entrepreneurs are often not heard when trade or competitiveness policies are made.

To address this problem, the chairman of the American Business Conference, Arthur Levitt, and I decided to survey our membership regarding their companies' international business. We already knew that about three-quarters of ABC firms derived significant revenues from abroad. Our thought was that a systematic examination of how international revenues are earned by some of America's most successful entrepreneurial companies might be of general interest and, perhaps, of use to policymakers seeking to broaden their perspective on the competitiveness dilemma.

"The Challenge of Global Competitiveness: Views of America's High Growth Companies" offers a full discussion of the ABC survey. I want here to mention a few of the more notable results:

* ABC companies are increasingly dependent upon foreign revenues as a fuel for their overall expansion. In 1982, 13.6 percent of the total revenues of ABC firms were derived internationally. In 1985, that figure had risen to 22.1 percent.

* Between 1980 and 1985, ABC firms increased their internationally derived revenues at a rate of 27 percent annually. ABC executives predict a similar growth for 1986 - 1990.

- ABC companies compete on quality, value, innovation, and service. They almost never compete on price alone.

- ABC executives reject the supposed primacy of labor costs in explaining this country's lack of competitiveness. They stress instead the importance of controlling total costs -- especially for market access, capital, and taxes.

- ABC executives oppose protectionist legislation.

- ABC executives believe that successful international competition is fundamentally a question of managerial will and skill.

As encouraging as these findings are, they should not be taken as evidence that ABC executives are sanguine about America's future in the international marketplace. The reverse seems true. Our survey revealed considerable distress among our membership regarding the related issues of the domestic deficit, an unstable monetary climate, increasing foreign indebtedness, and a relatively high cost of capital.

These issues, familiar as they are formidable, remain of first concern to the executives I represent. ABC members believe that the government is in a better position to do more for business's international prospects by a renewed battle against our fiscal and monetary problems than it is by passing legislation designed to police the trade policies of other nations.

This perspective is not unique to ABC members. While not all midsize and small businesses can claim international success of the sort enjoyed by many ABC companies, there is evidence of a commonality in outlook toward the challenge of competing overseas and the role government should assume in enhancing the competitiveness of American companies. On this point a 1986 survey of small business conducted by the Bank of Boston for this Committee is illuminating. The small business executives polled identified product quality and aggressive marketing as the chief prerequisites to a successful exporting strategy. They blamed adverse macroeconomic conditions, particularly an unfavorable exchange rate, for the recent decline in American exports. Finally, and perhaps most important, nearly 80 percent opposed the imposition of quota and tariff restrictions on foreign imports.

It would appear, then, that insofar as the national debate on trade and competitiveness has focused upon keeping foreign goods out of the American market, it could not be of less relevance to the constituency of this Committee. America's entrepreneurs are concentrating on penetrating markets abroad, and, in that context, sound economic reform, rather than protectionism, is the appropriate course for government to take.

This is not to say that artificial barriers to trade do not exist. They do. Our report lists those impediments to trade most commonly encountered by ABC executives. One of the most frequently mentioned is immediately amenable to governmental remedy: our own export licensing system.

Few issues have generated such needless controversy. No ABC member affected by export controls wants to do away with them. ABC executives do believe, however, that the process for obtaining an export license is unnecessarily cumbersome, especially for small firms, and marked by inter-departmental squabbling. The delay can cost sales since other nations administer their licensing programs more efficiently. Lost sales mean less money for research and development. Less R&D means loss of technological leadership. An unnecessarily restrictive or capricious export licensing system, in other words, is a kind of "reverse protectionism" that is no more to our benefit than its more traditional counterparts. We urge this Committee to support recent efforts to reform the export licensing system.

ABC executives also face foreign trade barriers. Given the remarkable record of international success enjoyed by ABC companies, it seems fair to assume that the foreign trade barriers identified in our report are real and not merely rationalizations for poor marketing or substandard products and services that no one in any nation would choose to purchase no matter how level the playing field.

ABC executives cited Japan, the European Economic Community, Brazil, and Korea as the nations with the most difficult barriers to American trade.

* Cultural Preferences were the most common foreign barrier to trade identified by ABC executives. Included in this category were the reluctance of talented foreign technicians to join American-owned subsidiaries, the tendency of governments to rely upon local suppliers, and the unwillingness of consumers -- both individuals and firms -- to buy American products and services. Japan and the member countries of the EEC were the nations most often associated with the cultural preferences barrier. ABC executives specifically singled out the EEC for domestic content requirements.

- Tariffs constituted the second most commonly cited trade barrier. Brazil is particularly notorious for its prohibitively high tariffs. ABC executives also fault Korea and Japan on this score.

- Discriminatory Regulatory Standards, a problem associated almost exclusively with Japan, was the third most commonly cited barrier. This category encompasses a variety of unpredictable, prejudicial, or unevenly applied regulatory policies.

Additional foreign trade barriers identified by ABC executives include: data flow restrictions, discriminatory tax policies, prohibitions against the repatriation of capital, and technology transfer requirements.

With omnibus trade bills introduced in the House and the Senate and with the Reagan Administration offering its own bill, it seems clear that trade legislation of some sort will pass this year. ABC executives firmly support the streamlining of current trade laws and the initiation of international negotiations aimed at lowering trade barriers. ABC executives are, however, suspicious of efforts designed to impose mandatory retaliation against countries registering "excessive" trade surpluses withthe United States. While viscerally satisfying, the impulse for across-the-board retaliation can hurt companies like those of the ABC in at least two ways:

- U.S. imposed restrictions on imports would directly harm the business of member companies who import the affected product either for resale, or as a component in a final product sold in the U.S. or abroad.

- If a trade war results from U.S. retaliation, the foreign country may erect new barriers against the sale of member companies' products or services in that country. Because ABC companies have been very successful in doing business in foreign countries, they are particularly vulnerable to such retaliation.

Trade retaliation is risky policy, a job for a scalpel, not a bludgeon. It is best done in specific, limited cases and only after full evaluation of any possible costs to American industry -- including those midsize and small businesses whose interests are often forgotten by those who would wield the big stick.

Mr. Chairman, you and your colleagues on the Small Business Committee are in a position to enrich the current, increasingly sterile debate on trade and competitiveness. By representing the interests of the entrepreneurial sector of the economy your Committee can, if it chooses, reorient the debate in a way that encourages success rather than simply protects failure. That means, specifically, resisting protectionism, promoting the reform of regulations, such as the export licensing system, that hamper the ability of American companies to export, and, most important, tackling the central macroeconomic problems of our economy that must, sooner or later, be addressed if we are to earn -- rather than borrow -- a standard of living commensurate with our citizens' rightful expectations.

PREPARED STATEMENT OF ROGER G. LITTLE, COCHAIR, NATIONAL INNOVATION NETWORK, AND PRESIDENT, SPIRE CORP.

STRENGTHENING AMERICAN COMPETITIVENESS IN WORLD MARKETS THROUGH THE SMALL BUSINESS INNOVATION RESEARCH PROGRAM

1.0 INTRODUCTION

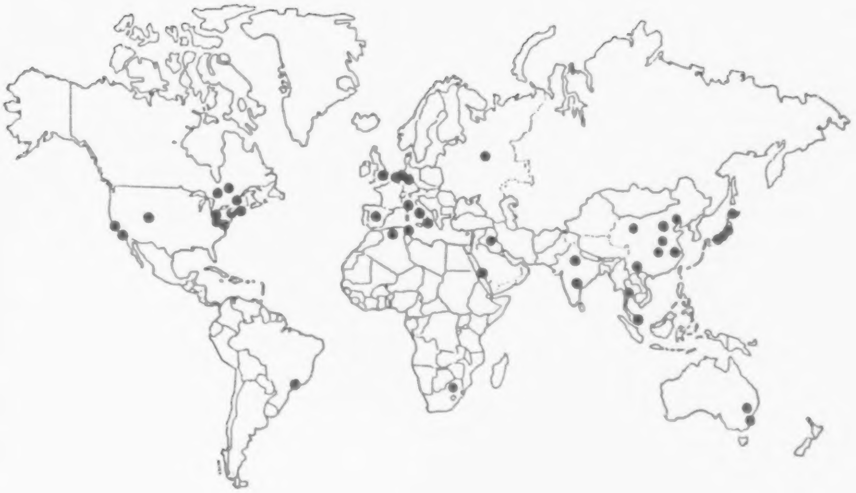
Spire Corporation was incorporated in 1969 and began doing government sponsored contract research and development work. Today, Spire Corporation, still a small business, is one of the world's leading suppliers of advanced semiconductor wafers; special processing machines; and processing services. Spire also provides services to industry internationally for the surface modification of metal components used in implantable medical devices, computers, and aerospace systems components. In addition, Spire is a world leader in photovoltaics (PV), having exported PV processing equipment to over 15 different countries throughout the world as shown in the attached map. We have therefore been quite successful in commercializing government-sponsored research for exportable products and services.

Based upon this experience we propose that small high technology businesses be mobilized for helping America win in the international market place. This mobilization can be achieved through an enhancement and appropriate direction of the existing Small Business Innovation Research program.

2.0 SBIR PROGRAM SUCCESSES AND WEAKNESS

The SBIR program, passed as Public Law 99-443, directs that Federal agencies to directly allocate 1 1/4% of their R&D budgets to small company competitions. This has been a very successful program involving hundreds of small businesses nationwide and demonstrated success in producing innovative new high technology products.

However, a major weakness in the SBIR program is that contracting is dominated by the Department of Defense's seventy-two (72) percent share of the federal research and development budget. Unfortunately innovative technology undertaken strictly for defense purposes is difficult to commercialize. These resources must be directed more towards consumer product spin-offs.



WORLDWIDE LOCATIONS OF SPIRE PV MANUFACTURING EQUIPMENT.

3.0 HOW TO MAKE U.S. MORE COMPETITIVE THROUGH THE SBIR PROGRAM

To achieve the objective of making the United States more internationally competitive and thereby improve our trade position, the following changes to the SBIR program are recommended:

(1) Increase the SBIR percentage of federal R&D from 1.25% to 3.25% in 0.5% increments over the next four years.

(2) Using one half of the increased funding increment each year, establish an SBIR commercialization policy for each Federal agency, including the Department of Defense, to commercialize the technology that is funded.

(3) Modify agency SBIR program solicitations to include development of innovative products which would be exports, such as to Third World countries, as well as competitive world-wide. Also allow development of innovative products that would substitute for present imports of consumer products from Japan, West Germany and other competing countries.

4.0 COMMERCIALIZATION OF DOD RELATED TECHNOLOGY

Even though some commercial spin-offs do result from Department of Defense R&D, these are generally fortuitous. The allocation of resources by the DOD to move technology to American consumer products would result in a much higher commercial application success rate. The Department of Defense is a strong proponent of commercialization of their technology. They should find this proposal attractive.

5.0 EXAMPLES OF WHAT COULD BE ACCOMPLISHED BASED UP SPIRE'S EXPERIENCE

The following examples illustrate what might be accomplished should these recommendations be implemented.

(1) Orthopedic Implants - National Institute of Health

Spire has developed a process for improving artificial hips and knees which are used in the human body. This process has been supported by the National Institute of Health and is finding wide acceptance in the orthopedic community. The devices that Spire processes are suited for the body size of Americans. The smallest size made is the largest size for the Japanese body. Spire is interested in developing innovative tooling for treating smaller components to be exported to the far east.

(2) Gallium Arsenide Semiconductor Wafers - Department of Defense

Spire is supported by the Department of Defense to develop new advanced semiconductor wafers for defense uses. In most cases these development efforts take the form of adding layers of atoms on top of semiconductor substrates such as gallium arsenide. The Defense Department is extremely concerned at this point that the principal suppliers of the substrates are the Japanese. The Defense Department therefore has begun to address initiatives to establish on-shore contractors. It would be in the Defense Department's best interest to establish a commercialization effort in order to fulfill their needs in the future. Although the military claims significant spin off to the commercial sector, directed commercialization efforts would yield much greater results.

(3) Ball Bearings - NASA

Spire has developed an advanced treatment using the ion implantation process for the surface of ball bearings to prevent them from wearing. This work has been supported by NASA's SBIR program. NASA, as well as the Defense Department, is quite concerned that the ball bearings are coming from overseas manufacturers. Examples are that Minibea has recently purchased New Hampshire Ball Bearing which is one of the major suppliers of bearings to the military community and the aerospace community. To help further commercialize this technology with American suppliers is in the best interest of NASA and the Defense Department.

(4) Photovoltaics - Department of Energy

The Department of Energy has supported Spire in developing advanced solar cells, i.e., photovoltaic devices which convert sunlight directly into electricity. The Department of Energy's mandate is to replace a significant fraction of imported oil for American electric utility demands. The problem is that with the present price of oil, the market for advanced energy technologies has dwindled in the U.S.

However, because about three quarters of the world's population does not have electricity, there is a growing need for photovoltaic solar energy in Third World countries to provide some basic needs such as water pumping stations, medical refrigeration, and village lighting. An SBIR commercialization program, from the Department of Energy, which addresses the export potential of its renewable energy technology products would be highly attractive to the Department of Energy and contribute significantly to our import/export imbalance.

6.0 SUMMARY

I believe that this proposal would mobilize one of American's greatest forces for winning in the international marketplace, small high technology business. I propose that these recommendations be incorporated into international trade legistations.

PREPARED STATEMENT OF MILTON D. STEWART, PRESIDENT, SMALL BUSINESS HIGH TECHNOLOGY INSTITUTE, PHOENIX, AZ, AND WASHINGTON, DC

With your permission, Mr. Chairman and Members of the Committee, I should like to present to you two businessmen who have one or two specific recommendations fo possible inclusion in a small business title for an international trade bill.

They are among the best and most thoughtful citizen-business people whom I know. Roger Little is President of Spire Corporation of Bedford, Massachusetts, one of the country's leading small businesses in several in innovative technologies, including the field of photovoltaics.

Mr. Little is Co-Chairman of the National Innovation Network which our Small Business High Technology Institute has been forming across the country.

* The views expressed in this statement are generally consistent with those of my fellow-members of Arizona Small Business United, and those of the Arizona delegation to the 1986 White House Conference on Small Business, to the extent that they represent issues that were before them.

** President, Small Business High Technology Institute, Phoenix, Arizona and Washington, D.C. Former Chief Counsel for Advocacy, Small Business Administration; President, National Small Business Association, President, National Small Business Investment Companies; Counsel and Presiding Officer, 1980 White House Conference on Small Business; Presidential Delegate, 1986 White House conference.

Gordon Johnson is former Chairman and CEO of Logetronics of Springfield, Virginia, a company which has now been acquired by another firm. He is presently Deputy Director of the nonprofit Center for Privatization. He was a member of the Virginia delegation to the 1986 White House Conference on Small Business. We are privileged to have him as a Director and member of the Executive Committee of the Small Business High Technology Institute.

Both of these men have had extensive experience with foreign trade. That alone marks them as unusual among American entrepreneurs who have managed small businesses. Their advice to you will be far more strongly based on first-hand business experience with overseas trade and meeting foreign competition than mine can be. All three of us have studied the Federal Small Business Innovation Research program. (Mr. Little's company is an outstanding performer in it.) We have not prepared our testimony together.

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1. A small business title in the proposed trade bill should make it a clear, permanent and pressing goal for the USA to expand the small business share of the emerging global economy's international trade.

For more than forty years — ever since World War II, our country has followed the traditional pattern of other countries — world trade is an instrument of national geopolitical policy.

That means (in other countries) that it is almost entirely the business of government-owned and managed companies or (in our country and our closest allies), government-sized private companies, or a combination of the two. That is one of the two sources of our present plight — 85% of US export is done by fewer than 2500 companies. Many thousands of American companies should ideally be participating, but are not. In this, as in every other significant area of public policy (with a few exceptions), Federal policy treats large, small and mid-sized companies "equally" — meaning the same way. Wherever and whenever that happens, it means heavier burdens for small companies and more help for large ones.

In the past ten years, we have seen dramatic evidence of the price we pay for excessive reliance on a few large companies' competitiveness. The industries in which foreign competition has most successfully devastated American companies in our domestic markets have first been characterized by excessive concentration.

The second source of excessive reliance on large firms -- and it is tied to the first one -- is American small business' disinterest in foreign trade. Ours is the only domestic market in the free world big enough to allow a small company to grow as much as most small companies want to grow without ever becoming involved in foreign trade. The Federal government has failed, thus far, to develop an international small business trade program that works. That has simply reinforced small business' judgment that it is so much easier to grow in our domestic market that it just makes no sense to become involved in foreign trade.

Two things are changing this, both within our own country and abroad. At home, more and more small companies have felt the adverse impact of foreign competitors' success. In many parts of the country, they have seen major company plants cut back or shut down. And they have felt the effect of sourcing shifts out of the country by large companies in the U.S., whether owned by foreign interests or domestic ones.

In the 1980 White House Conference on Small Business, no subject dealing with international trade got as many as 300 votes of a possible 1600 — five recommendations considered ranked between 31st and 55th of 60. (See Appendix 1).

By the time of last Summer's 1986 White House Conference on Small Business, concern had risen so that a combination foreign trade recommendation ranked fifth of sixty. Naturally, but unfortunately in my opinion, it focused on Federal organization and management of foreign trade, an issue which is so long-term, based on past experience, as to make it almost irrelevant.

A second factor making this a good time for a sharp and visible national priority shift towards small business trade participation is the climate of opinion in other countries. Our vigorous job-making small business sector is the envy of Europe and the rest of the world. They have seen us create millions of jobs, starting hundreds of thousands of new entreprises while their employment stagnated and joblessness rose. They saw our small business sector create more than enough jobs between 1980 and 1986 to compensate for more than two million jobs lost by large companies, and thus help to pull us out of a recession.

In Western Europe, in the advanced Pacific rim nations, in Eastern Europe — more and more serious attention has been given to the value of small business to domestic economies. Our White House Conference in 1980 was attended by a small number of Western European observers. They went home with a fresh determination to start the European Community down the small business road. They stimulated one of the first actions taken by the first popularly elected Common Market Parliament — to declare 1983 the "European Year of Small and Middle Sized Enterprise" (EYSME). All through that year, in every member nation, there were meetings, studies, conferences, seminars on how they could build an American-style small business sector. Since 1983, the EEC continued to move towards making a strong small business sector a central concern of its member nations.

In Communist China, the present leadership reports that there are now 7 1/2 million private small businesses — almost all tiny, family businesses. In the Soviet Union, beginning in May, State and State agency employees will apparently be allowed to engage in certain specified private self-employment activities. This hardly represents a conversion to an entrepreneurial economy as we know it; in both countries they struggle to find a way to allow small business to exist while maintaining the Communist Party's iron political dictatorship. That is why they swing between moves towards "economic reform" and "liberalization" and crackdowns on "Western" and "capitalist" cultural and political heresies. They'd like the efficiencies and innovations of economic entrepreneurship without the political liberty that has always accompanied it elsewhere. They will find, in time, that you just can't have one without the other.

The climate at home and abroad is generally right for a move towards a stronger, more enduring Federal commitment than we have ever had to a virgorous international small business sector. A small business title in the trade bill can both articulate it, and provide for accountablility to the Congress for an intensive effort to achieve it. But it will take, in my opinion, at least one other step, to start us down that road.

2. We badly need a "Summit Nation" international equivalent of our White House Conferences on Small Business. A small business title of the 100th Congress trade bill could and should be the first bipartisan step toward such a conference.

This is one of the recommendations of the National Commission on Jobs and Small Business. Chairman LaFalce was one of the Congressional convenors of that 18-member group; Presidents Ford and Carter served as its honorary chairmen. I am proud to have been a member of it, and commend to the members of this Committee its report ("Making America Work Again") and its recommendations. They will be discussed by at least one other witness before the Committee.

This particular recommendation, however, should be so central to a small business title in a new trade bill that I cannot pass up the chance to discuss it.

In terms of small business leadership, organizations, consensus on a wide front -- on foreign trade, in government and out, we are today about where we were on domestic small business issues in 1978. Few would deny that the 1980 White House Conference on Small Business resulted in a forward thrust for small business in many areas. Its effects are still being felt within the Federal and State governments. A study of its effectiveness by the Senate Small Business Committee staff estimates that 80% of its recommendations had been carried out in whole or part by 1984.

We need a similar "watershed" conference on foreign trade run by small business itself in which it arrives as its own consensus about international and national institutional and policy needs. To be meaningful and effective in building an international small business sector capable of long-term growth, the Conference must itself be an international one, with delegates from the principal advanced nations — those with the most developed small business sectors.

it must be sponsored and convened by an international body with official standing; we need a conference to which governments themselves will listen. That means they must have a hand in calling it, but not in deciding or influencing its recommendations; those must come from small business people themselves. Our White House Conferences were, I think, a good model for delegate selection — about two-thirds of the delegates elected at open meetings of small business people and one-third chosen by the Congress and the President.

There is no reason that I can see that the same principles could not apply in Canada, the United Kingdom, France, West Germany, Italy and Japan. Since the EEC is represented independently at Economic Summit meetings, there could be a single delegation for its other members: (Ireland, Belgium, the Netherlands, Denmark, Greece, Luxembourg, Portugal, and Spain.)

That would leave out most of the EFTA (European Free Trade Associations: Austria, Iceland, Norway, Sweden), Finland, Turkey and Yugoslavia. It would also leave out the Third World nations and the Communist bloc. All of them could have "observer" status. To go beyond the Summit nations at a first conference makes the problem of reaching consensus far more difficult.

The Conference would have as its very specific purpose making recommendations for changes in the laws, policies and regulations of the nations represented to expand their trade with one another in ways which would specifically expand the size of the small business sector in that trade. The recommendations could cover a possibe "GATT for small business," bilateral or multilateral international small business agreements or institutions or home economic policies to contribute to the goal of the Conference.

Preparations for such a Conference should be in the hands of a specially-named Commission in each Nation. Every effort should be made to make the management of such a Conference even more independent of internal political influence than our White House conferences. In our country, membership of a preparatory Commission should be scrupulously bi-partisan, named in part by the President and in part by the leadership of both parties in each House of the Congress. Staff should function outside the Executive branch and the Congress, but draw on both for help.

My guess is that it would take two to three years to prepare for such a Conference within and among the participating nations.

This year the Economic Summit will be held in Venice in early June. Statements issued at the last two Summits (Bonn in 1985 and Tokyo in 1986) are encouraging as reflecting the growing interest in small business of the Chief Executives of those Nations. (See Appendix 3). It seems to me that if the Congress encouraged or joined with the President in an initiative for such a Conference before June there is a good chance that it might be called at the Venice meeting — or if that's too close, the 1988 Economic Conference.

Haven't there been conferences of small business people from different countries? Yes, but not under the auspices and with the specific mission I've suggested.

What would American small business and our government get from such an international conference that woud make it worthwhile?

First, a clear sense of where American small business people and those in the most important other countries we must live with agree and where they disagree. Second, better prepared answers from better-informed small business people about what will work and won't in expanding world small business trade. Third, if it works well, a wide consensus and an effective constituency for what affected small businesses really want.

Our country will get one other thing. Ours is by far the largest small business sector in the world. It's share of employment, and gross domestic product is far larger than the people of the rest of the world — and plenty of Americans — realize. Too often we are viewed only as a nation of large companies and a mammoth civilian and military bureaucracy. Whether we will be seen more accurately if we join in initiating such a conference will probably depend on the outcome. But I believe we will.

3. We need a major Federal-State initiative to strengthen small business participation in foreign trade. A small business title in the trade bill may be a good way to launch it.

Ever since 1980, there has been an increasing focus in the States on their own small business sectors. More and more of them are giving priority to the expansion of their home-grown businesses to balance their continuing efforts to persuade companies or entrepreneurs from elsewhere to set up shop within their borders.

At the same time, to be perfectly blunt, the Federal government has been giving signals that shout "overload" for some years now. In several key areas, it is deadlocked or gridlocked in ways that may limit its policies and managerial freedom in the immediate future. There are areas in which stronger or new incentives — particularly financial ones — have costs that can properly be shared. In many ways, the States and their municipalities are closer to small business than the Federal government. Often it has seemed to me that the best way out of Federal interagency conflicts of jurisdiction or program in small business would be to let the States do the actual management or administration of a program. A number of States are already at work on their own in small business foreign trade work. What I'm suggesting is more than "cooperation" between two or three levels of government personnel. One example beyond that would be a shared guarantee of long term loans to make more bankable small companies with weak balance sheets but others able and willing to export.

The Federal deficit means that almost any significant (or even insignificant) expenditure or obligation proposal will have to run a protracted gauntlet of tough opposition. In the present climate, it will not be easy to make effective starts at improving on things like the Export Trading Corporation. The lengthy trauma of the effort to abolish the Small Business Administration pre-empted time which should and could have gone to the serious issues you are now addressing. That trauma has left scars. Once again we await the early confirmation of a new SBA Administrator. He's entitled to, and it's prudent to give him some time to find his feet. Perhaps he will give SBA and the Executive branch stability and leadership in this area.

It is certainly appropriate and not a waste of time for this Committee to explore the possibility of a good Federal-State incentive initiative. The bulk of the actual work should be done in the private sector and the government work and risk shared between the Federal government and the States. I would not try to find the exact program in time for the drafting of the small business title of the trade bill. All I would try to do in that, given the time pressure and the other factors I have mentioned, would be to lay a solid conceptual basis for it in the enactment, and spend the next year working with the States and the Executive branch to develop it.

4. Despite the urgency of the problem, the specific program scope of the proposed Title should be limited. It can be followed with separate supporting legislation over the next 18 months.

There is much that needs doing to strengthen small business at home and abroad. You already have before you the recommendations of two White House Conferences on Small Business. You already have before you the recommendations of the 18-member National Commission on Jobs and Small Business. You may be sure that our Institute and the leadership of our Network are ready to help you with opinions on priorities, choices among approaches or in any other way our limited resources will permit.

What obviously concerns me is that historically, trade bills have, not always been the best vehicles for drawing together all the elements of the small business community, much less the Congress or the whole Federal government. Small business must look to this Committee and its opposite number in the Senate, as it always has, to be a vigilant guide for other Congressional committees where small business is concerned. Some parts of the small business community have been hurt badly both directly and indirectly by foreign competition. That is especially true of some parts of the country. What they want from the Federal government is help that other parts of the country and small business consider to be self-defeating protectionism. Others are in some profitable foreign trade catbird seat. They want no change in the status quo. They talk about protectionism beggaring us or our neighbors, but forget that one-sided "free trade" policies can do the same thing. Free trade as a national and world goal does not require us to be improvident or stupid in a world that is not yet all free.

One great contribution this Committee can make is to recast the trade issue from protectionism versus free trade to what is really the issue for small business. What we need are (1) effective reciprocity with the rest of the world; and (2) a stronger national commitment everywhere to the expansion of small business sectors, both at home and internationally.

5. The Federal Small Business Innovation Research (SBIR) program deserves special consideration (for new Members of the Committee, we have appended a brief description of it - Appendix 5). An increase in the program size is justified for the following reasons:

a. Appendix 4 indicates how seriously the technology base of our country has been affected by foreign competition;

b. Most economists share John Kendrick's estimate that 40% of productivity improvement is attributable to technology.

c. The Federal SBIR program does not add to expenditures; it directs a small amount of dollars already committed to be spent to the ablest small technology-based businesses on a competitive basis. It is wholly within the control of the Federal government. It will provide more scope for a broader geographical participation in the program. It will provide more room for universities and non-profit institutions to participate. It can and should provide room for far more flexibility among the agencies administering the program.

d. The first four years of the program were, we believe, promising enough to justify a prompt and modest expansion of the program. Both the 1986 White House Conference and the National Commission on Jobs and Small Business concurred in the recommendation.

e. Although there are aspects of the program still to be fully tested, we have seen enough promise to believe it is urgent to increase the program's size.

We will be glad to help this Committee, its staff or anyone else in the Congress to speed favorable consideration of the recommended increase from 1.25% to 3% of extramural Federal procurement.

As always, if there are other matters on which the Committee would like comment, or if anything said in this hastily prepared statement is unclear, I will be pleased to add to it or explain in a supplementary note.

APPENDIX 1: WHITE HOUSE CONFERENCE ON SMALL BUSINESS 1980 RECOMMENDATIONS WITH DELEGATE VOTES

15 TOP PRIORITY

1. (1,129 votes) Replace the present corporate and individual income tax schedules with more graduated rate scales, specifying the graduated corporate tax scale up to $500,000

2. (818 votes) Adopt a simplified accelerated capital cost recovery system to replace the present complex Asset Depreciation Range (ADR) regulations, with provisions such as (A) immediately expensing capital costs less than a specified amount, (B) immediately expensing government mandated capital costs, and (C) the creation of a maximum annual benefit that may be derived from the system

16. (807 votes) Balance the Federal Budget by statute in Fiscal Year 1981 by limiting total Federal spending to a percentage of the GNP commencing with 20% and declining to 15%

3. (799 votes) Revise estate tax laws to ease the tax burden on family-owned businesses and encourage the continuity of family ownership

41. (757 votes) Congress shall exercise its oversight function with the assistance of the General Accounting Office, instituting sunset reviews of all laws, regulations, and agencies, to ensure that none exceeds original congressional intent. Sunset reviews, in an appropriate time frame (not less than every five years), should include economic impact analysis and proposed agency budget reductions, leading to re-enactment of each agency's enabling legislation to permit its continued existence, or to reduce its size and cost

(a) Establish a Regulatory Review Board composed of representatives from the Executive Branch, Congress and small business owners with responsibility for impact statements and cost controls

(b) Congress shall exercise [illegible] regulations within a specified time [illegible] congressional oversight committees [illegible]

11. (746 votes) Support and urge passage of S 1860, the Small Business Innovation Act of 1979, and companion bill H R 5607, as presently drafted with flexibility for minor future amendments, covering small business research and development set asides, small business innovation and research programs (as already encompassed by H R 5126 and S 1074), patents, retention, amendments to the Internal Revenue Code, and regulatory flexibility

4. (681 votes) Provide for a tax credit for initial investment in a small business, and permit deferral of taxes for roll-overs of investments affecting small businesses

17. (675 votes) Reform the Social Security System by including, where constitutionally possible, all public and private sector employees as contributors, and more closely tie benefits to contributions to move the system toward actuarial soundness. Limit benefits to the original old-age and survivors benefits. Freeze the tax base and tax rate at the January 1980 level. Eliminate double dipping

5. (546 votes) Provide tax incentives in the form of a new security called a Small Business Participating Debenture (SBPD) to provide a source of capital for small businesses

47. (597 votes) The Office of Advocacy must be maintained, reinforced and expanded so that activity be not less than 5% of the SBA salary and expense budget. The legislative mission of Advocacy must be considered the number one priority of SBA and the Office of Advocacy. The independence of that function of the Office of Advocacy must be protected so that it may continue to have the confidence of the small business community. SBA's Advocacy budget should be devoted to economic research and analysis, as well as small business advocacy. Small business advocates under the direct supervision of the SBA Office of Advocacy, shall be assigned to OMB, Federal Reserve Board, Treasury, International Trade Policy Committee and other regulatory agencies

36. (578 votes) Private lending institutions should be required to provide equal access to commercial credit for women in business. The Federal Reserve Board should establish record keeping requirements for commercial loans to women which will permit effective monitoring of performance under the Equal Credit Opportunity Act. The Small Business Administration should make bank certification available to as many commercial banks and other lenders as possible and establish targets for increasing the dollar volume of loans made to minority-owned and women-owned businesses as one of the criteria for recertification

42. (564 votes) Small business should be eligible for magistrate review of agency civil penalties, and reimbursed for court costs, reasonable attorney's fees, and damages from administrative action, if successful in civil disputes with the Federal Government, including IRS

(a) Such costs and fees to come from the operating budget of the agency

(b) Magistrates will be appointed and be responsible to the judges in each Federal Judicial District

(c) With burden of proof on the agency to defend its action

18. (553 votes) Revise minimum wage standards by freezing standards at January, 1980 levels and establishing a two-tier minimum wage by exempting teenagers, seasonal workers and part time workers

6. (472 votes) The President, by Executive Order and Congress, by legislation, shall establish mandatory goals for *all* Federal procurements and Federal funds or grants to states, localities, and public and private institutions, on a contract-by-contract or agency-wide basis for small businesses (35%), minority-owned (Black, Hispanic, Native American, Asian Pacific American, and other racial minorities) businesses (15%), and women in business (10%)

46. (471 votes) Require that all government agencies which develop fiscal, monetary, legislative and regulatory policies/practices shall submit small business "economic impact" statements that require the regulatory agencies to identify the anticipated benefits and to justify the costs of Federal regulatory requirements to small business. In addition, all regulatory policies shall be subject to sunset provisions to be reviewed every 5 years in order to ensure that only cost effective regulations shall be maintained and retained in the future

International Trade

51. Congress should broaden the tax deferral options of the Domestic International Sales Corporation and provide for the development of an American Trading Company which would automatically qualify as a DISC. Tax deferral options should include the following additional provisions for DISCs: (1) allow for deduction of twice the monies expended for participation in any bona fide overseas trade fair by a DISC, (2) allow for deduction of twice the amount of premiums paid to Eximbank and FCIA, as legal deductions prior to payment of DISC taxes, (3) increase the $100,000 exemption clause to $500,000, (4) provide for a graduated tax on "deemed distribution" from $500,000 for $50 million, and a standard rate of 50% levied on over $50 million, (5) exempt new DISCs from any "deemed distribution" requirement for at least the first three years of operation, and (6) provide for the elimination of existing incremental provision of DISC regulations. Congress should provide within the tax structure an "Exporter's Allowance" or tax deduction which would apply in the trade of all goods abroad by granting an allowance for 75% of the marketing expenditures incurred by the exporter.

(297 votes: 31st)

52. Eximbank should establish a special small business funding program through commercial banks, and should consider discounting loans to support international sales and should develop a cooperative program with the SBA for pre-export financing.

(53 votes: 55th)

53. The Federal government should establish field one-stop service shops to include export services of all Federal agencies under the guidance of the Department of Commerce.

(68 votes: 52nd)

54. The President and Congress should consolidate under an existing cabinet level department, a unified world trade administration. It would be responsible for all trade policy functions of the various agencies and departments. Its objective would be to maximize the international competitive strengths of U.S. Small Business with support and goals for minority, women-owned and disadvantaged business and specific programs developed to utilize their units of technological, educational, cultural, language and political expertise.

(117 votes: 42nd)

55. Congress should provide for support and expand the use of all officially recognized Trade Fairs, Exhibits, and Trade Centers abroad with small business participation, continue to encourage the Department of Commerce to increase the promotion of foreign buyer and foreign visitor travel to the United States, and develop a program utilizing the cultural, language and political expertise of all Americans, especially ethnic groups, to assist in preparing, implementing and utilizing a sales package for use in expanding International Trade in all world markets.

(251 votes: 36th)

APPENDIX 2: FINAL SELECTED RECOMMENDATIONS-- White House Conference on Small Business 1986

(These are the principal recommendations of the 1986 Conference which appear relevant to the matters dealt with in the Statement. Reference should be made to all 60 which were published to be sure that inadvertent omissions have not been made.)

5. The international trade crisis mandates the creation of a Cabinet level department of international trade (similar to that of our major trading competitors), which will coordinate and focus on existing activities of federal agencies to accomplish the following:

a. Coordinate the dissemination of information regarding business opportunities, export financing, education and training, licensing, trade missions, market-driven data bases, SIC Code updates, and other essential functions of international trade.

b. Represent small manufacturing, agriculture, service and other businesses, in national and international discussions and negotiations. Develop and execute fair, long-term policies regarding international trade.

c. The General Agreement on Trade and Tariffs (GATT) should be extended to include intellectual property rights, services, agriculture, aqua-culture, and agri-business products. [R.A. 142, International Trade; 1173 votes]

14. The Senate and tha President should join the House of Representatives in re-authorizing the Small Business Innovation Research (SBIR) Program by enacting H.R. 4260 before the present Congress adjourns. The next Congress should strengthen the program still further by:

a. Increasing each agency's share of R & D expenditures devoted to it by .25 per cent per year, until it is three percent of the total extramural R & D Funds;

b Making the program permanent with a formal congressional review every ten years beginning in 1993;

c. Allocating a modest, but appropriate share of each agency's SBIR fund for administrative purposes for effective management, quality maintenance and the elimination of program delays;

d. Determining annually that each agency is clearly in full compliance with the law and that SBIR program funding is not being accompanied by parallel reductions in other small business programs, and

e. Creating pooled solicitations once or twice a year of subjects submitted by small agencies expending $20 million to $100 million in extramural R & D funds to facilitate their involvement in the SBIR program. [R.A. 125, Innovation; 1043 votes]

15. Protection of intellectual property in the form of patents, trademarks, copyrights, technical data and deliverables, is critical to the growth of small business. Federal government and their contractors should be required to honor confidentiality for protecting domestic intellectual property nationally and internationally. To that end,

modifications and additions to existing systems are necessary

a. Implement a system by which a U.S. small business may elect an accelerated, short-term, patent filing and approval procedure by simple registration.

b. Make the tiered fee schedule within the patent office more equitable by charging fees for information and services as well as for filing and maintenance; and by setting fees which are lower for first filings of national patents than filings by foreign patentees.

c. Establish an accelerated judicial procedure within the district courts which utilizes patent and trademark expertise and thereby expedites litigation concerning patent and trademark infringement.

d. Recommend the President and Congress work toward the establishment of coordinated filing in the Western Hemisphere and Pacific Rim Countries.

e. Develop a set of verifiable and enforceable copyright procedures to strengthen enforcement of U.S. copyrights, in both domestic and international markets, through the joint efforts of the Copyright Office and the private sector, including representation by small business.

f. Laws and regulations regarding proprietary rights in technology and "rights in data" on government contracts shall be changed to allow small business to maintain its proprietary rights.

g. The Freedom of Information Act should be amended to shift the burden to the requestor for obtaining release of proprietary and confidential information.

h. Congress shall collect data and analyze new technologies being developed to assist them in enacting appropriate legislation for the expansion of the intellectual property law system to adequately cover these new technologies.

i. Establish a management oversight group, to include small business people, which ensures efficient and effective implementation of the intent of the patent office mandate to be a national resource. [R.A. 129, Innovation: 1034 votes]

30. In order for American business to compete in foreign countries with other nations we need to clarify the Foreign Corrupt Practices Act. Congress should pass legislation similar to language in S. 1860, Title IX, Subtitle B:

a. The name of the act will be The Business Practices and Records Act.

b. Willful bribes to any foreign officials will remain prohibited.

c. United States companies will be liable if they corruptly pay a bribe directly or if they directed or authorized the bribe "expressly or by a course of conduct."

d. All exceptions will be codified including those that are explicitly stated as well as those which have been permitted under the present law.

e. Payments made "for the purpose of expediting or securing the performance of a routine governmental action" will not be unlawful.

f. Payments which are expressly permitted by law, custom or regulations of a foreign country will not be unlawful. [R.A. 15[illegible] International Trade: 666 votes

34. Unemployment Insurance. amend the Federal Unemployment Tax Act and the Social Security Act and the Wagner-Peyser Act to achieve the following.

a. Prohibit strikers from collecting benefits.

b. Require claimants to actively seek work and accept the next best job after eight weeks of job search or lose benefits.

c. Eliminate FUTA and related taxes on wages of persons who do not qualify for benefits, (e.g., independent contractors, corporate officers, share-holders, retirees, etc.)

d. Allow surplus funds to be invested in the state which paid the taxes.

e. Cap FUTA tax at present levels.

f. The rate increase of .2% in FUTA taxes should be allowed to expire on January 1, 1988 as scheduled under current law. [R.A. 244, Payroll Costs: 654 votes]

35. "Export S.B.I.R."
Increase exports by small business by:

a. Creation of an annual, competitive small business export incentive program similar to the highly successful SBIR* Program, to be funded within existing International Trade Programs,

b. Retention and improvement of the current Small Business Foreign Sales Corporation tax incentives to further encourage exports of products and services, and

c. Aggressively market small business export trade programs using private sector organizations or businesses.

*The Small Business Innovation Research approach is a competitive annual program which solicits small business proposals to solve problems instead of responding to government solutions. It offers a significant multiplier effect, requires no new government funding, and requires a commitment of private sector funds. [R.A. 156, International Trade: 600 votes]

39. Adopt a basic economic policy to continually improve our economic climate by removing obstacles to our free enterprise system and allow it to function with minimum government restraints. This national economic policy should be instituted to phase out all governmental pricing, production, and export controls currently imposed on U.S. business. Include deregulation of the energy industry by decontrolling natural gas, removing the foreign policy-based controls on the export of natural resources and oil field service equipment, and by reducing bureaucratic barriers to U.S. petroleum exploration and production efforts. And finally, deregulate the steel industry. [R.A. 22, Economic Policy: 560 votes]

40. Recommend that the nation's farm policies be changed to facilitate a phaseout of price supports and governmental production controls, within an established time frame, thereby returning agriculture to a market orientation, while bringing all pressures to bear in the General Agreement on Tariffs and Trade (GATT) deliberations to insure that other importing and exporting nations adhere to policies which promote free and fair trade in agricultural commodities. [R.A. 20, Economic Policy: 557 votes]

Appendix 5 : The Summit Nations and Small Business

Following the first White House Conference on Small Business in 1980, the first elected European Parliament declared 1983 as the European Year of Small and Medium-Sized Enterprises (EYSME). Each of the member nations of the European Community held a year of conferences and policy research sessions studying how to expand its own small business sector A European Community meeting in Strasbourg concluded the Year. At the 1985 Summit Conference in Bonn, Germany, four participating nations made statements setting a high priority on small business growth in their domestic economies.

Great Britain	"The Government of the United Kingdom...will promote the development of small and medium-sized businesses and advanced technology industries, and encourage initiative and enterprise and the creation of new job opportunities."
Germany	"The Government of the Federal Republic of Germany attaches high priority to strengthening the flexibility and vigor of the economy in order to achieve a lasting improvement in growth and to create new jobs. Small and medium-sized businesses should be especially encouraged as well as high technologies."
Italy	"The Italian Government....particular emphasis will be put on incentives to create small and medium-sized industries, especially in the field of high technology, and to promote employment, especially for young people."
Canada	"The Government of Canada...will encourage entrepreneurial activities, with emphasis on the small and medium-sized business sectors."

At the 1986 Summit Conference (May in Tokyo), all the Summit Nations (the four above plus the US [President Reagan], France, Japan, and the European Community representatives) joined in a closing statement which included this paragraph:

> "Since our last meeting we have had some success in the creation of new jobs to meet additions to the labor force, but unemployment remains excessively high in many of our countries. Noninflationary growth remains the biggest single contributor to limitation and reduction of unemployment, but it needs to be reinforced by policies which encourage job creation, particularly in new industries, and in small business."

That statement, brief as it is, is a high-water mark for small business internationally. It is the first unanimous recognition of the research data from a number of countries — above all ours — showing that small firms create the bulk of the new jobs and much of the industrial innovation. Yet the growth prospects of small firms will be tied more and more to foreign trade which continues to explode as a factor in the economies of all the industrially advanced nations.

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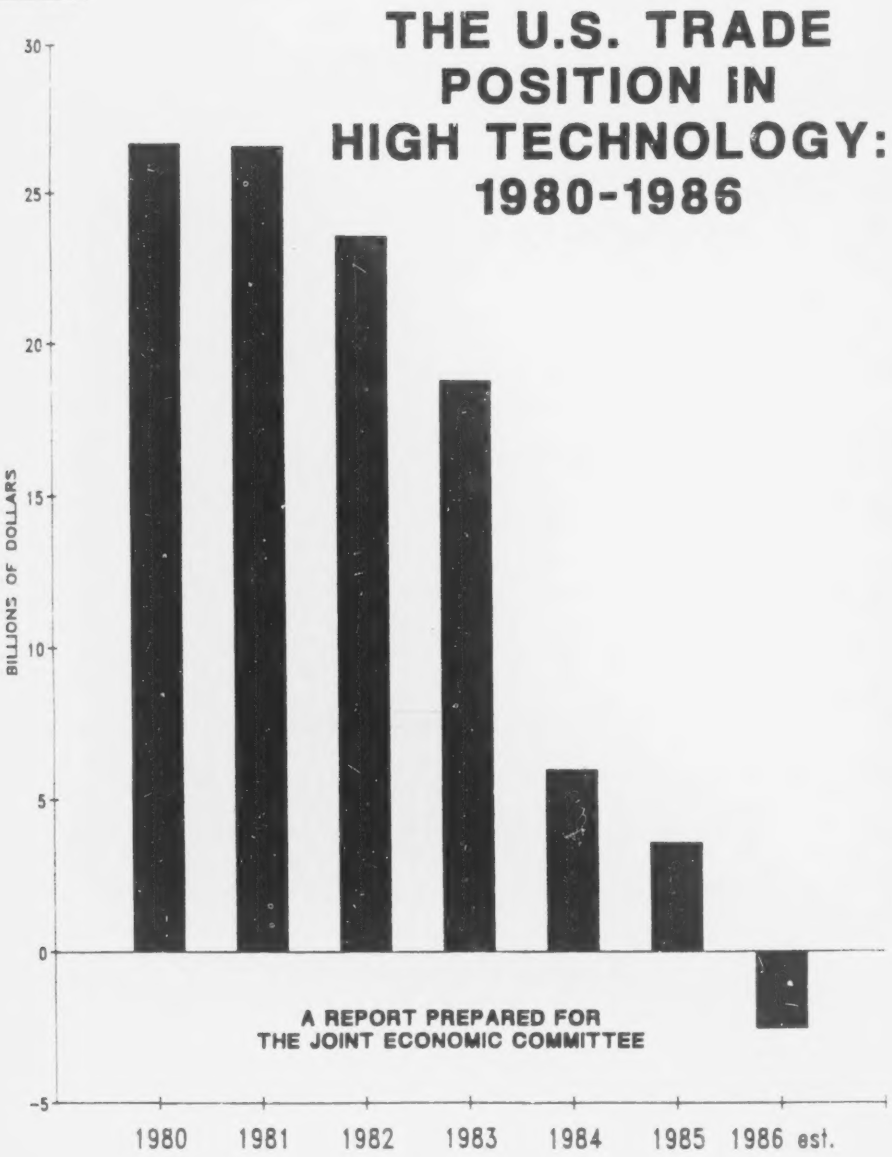
In every country — but especially in the USA — foreign trade has been primarily the business of large companies and large government agencies. In the smaller countries, small firms have had to be "foreign-trade-minded" because their home markets did not provide much room for growth. The USA as the largest integrated market in the world has provided plenty of room for small USA firms. But now, small USA firms face growing competition in the the US market from more and more foreign firms, large and small. Active cultivation of exporting has been increasingly urged on small US firms by Federal spokemen deeply troubled by the over $150 billion dollar US foreign trade deficit. Yet an estimated 85% of US exporting is done by fewer than 2,000 large firms. "For total merchandise exports, 10 per cent is accounted for by five exporters, 27 per cent by 50 exporters, and over 70 per cent by about 1000 exporters. For manufactured goods exports, 13 per cent is accounted for by five exporters, 34 per cent by 50 exporters, and over 60 per cent by about 1000 exporters." "Only an estimated 30,000 ou of a total of 376,000 manufacturing companies currently export." (Report of the President on The State of Small Business, pp 299 and 298, March 1984.)

APPENDIX 4

THE U.S. TRADE POSITION IN HIGH TECHNOLOGY: 1980-1986



A REPORT PREPARED FOR
THE JOINT ECONOMIC COMMITTEE

Appendix 5

THE SMALL BUSINESS INNOVATION RESEARCH PROGRAM

What is the Small Business Innovation Research Program? It is a federal program that requires federal agencies and departments to allocate part of their R&D budgets to certain small company competitions. Until enactment of the Small Business Innovation Development Act on July 22, 1982, only the National Science Foundation and the Defense Department had such programs. Now at least nine more Federal agencies have such programs. They are: The Departments of Energy, Health and Human Services, Agriculture, Commerce, Transportation, National Aeronautics and Space Administration, Nuclear Regulatory Commission, and the Environmental Protection Agency.

Public Law 99-443, passed almost unanimously by Congress and signed by the President on Monday, October 6, 1986 continued the program to September 30, 1993.

What kinds of companies participate in SBIR? Companies with one to 500 employees that have strong research or R&D capabilities in science and engineering are eligible. Companies with 10 or fewer employees have won more than 1/3 of all awards. SBIR, however, is not an assistance program for small businesses. It is highly competitive and merit based. Only companies doing high quality R&D will win. To date, only 1 out of every 8 proposals has been funded in Phase I; only 1/3 of these received Phase II grants.

How does the program work? In Phase I, Federal agencies issue a solicitation bulletin one or more times a year. Here they list research problem areas or topics on which they would welcome proposals from small companies. Phase I gives grants of up to $50,000 for R&D studies. Only Phase I winners may submit Phase II proposals. These grants are designed for full scale R&D; they are for 1 to 2 years and may be as much as $500,000.

In Phase III, companies can pursue any potential commercial applications either with private funding or through government production contracts. Phase I and II provide full allowable costs and a negotiated profit for the company. The program does not fund private commercial development; that's for Phase III.

Why is this program unique? It is aimed at markedly improving the opportunities for small companies in Federal R&D, while boosting the economy. The NSF program, which is intended to serve as a model, asks the proposer if the R&D has potential commercial applications and whether the small company intends to pursue these applications with private investment in Phase III. When proposals are judged about equal in technical quality, those that have commercial potential will receive Phase I awards. Before applying for Phase II, the Phase I winners are asked to obtain contingent commitments for private funding at least equal to the amount requested from the government for Phase II.

How big is the program? The 1982 law expanded SBIR into the agencies that do 99% of all federal R&D. By 1987, assuming continued growth in R&D, the program should be funding about $400 million annually with small technology-based businesses. In the next seven years, at the present legally required set-aside rate, more than 2 1/2 billion dollars is likely to be available.

How many R&D projects will be funded annually? By the fifth year there should be about 2,500 SBIR projects each year, with more than 1,500 in Phase I and about 750 in Phase II.

Who receives patent rights? World-wide commercial rights to any patents normally will go to the small company. The government will retain rights for government use, and if the company makes no effort to commercialize the results, the government in time, will retain still other rights.

Are small non-profit organizations eligible? No. The program is solely for small businesses. The program also requires that the R&D be carried out in the small business and that the principal scientist or engineer on the project be primarily employed by the small company at the time of the award.

Where do the companies get the private funding commitments for Phase III? Usually from venture capital or manufacturing companies already in the field that are seeking new products or licenses or investment opportunities. The commitment is not required for Phase I funding. At Phase II it may be decisive between two tied competitors.

Who can tell when a specific agency competition opens and closes? The Small Business Administration has responsibilities for coordinating the program. To receive the SBIR information as soon as it becomes available, write to: U.S. Small Business Administration, 1441 L. St., NW, Washington, D.C., 20416 (Office of Innovation Research and Technology, Rm. 500). It will normally come in a "Pre-Solicitation Announcement" mailed to you quarterly. A list of agencies which will make offerings in the next quarter is given along with the dates of release of the Agency's solicitation document and the dates of closing submission. The quarterly gives a one-line statement for each topic in the solicitation. Ask SBA to be put on the list for regular mailings of the quarterly.

While the SBA's document is useful, each agency's own solicitation is the best, fullest source on each competition. Attached is a list of direct sources from which to request them.

TRADE AND COMPETITIVENESS ISSUES

THURSDAY, MARCH 19, 1987

House of Representatives,
Committee on Small Business,
Washington, DC.

The committee met, pursuant to notice, at 1:03 p.m., in room 2359-A, Rayburn House Office Building, Hon. John J. LaFalce (chairman of the committee) presiding.

Present: Chairman LaFalce; Representatives Mazzoli, Cooper, Olin, Bilbray, Flake, Lancaster, Campbell, DeFazio, Price, Slaughter, Gallo, Baker, and Rhodes.

Chairman LaFalce. The committee will come to order.

This afternoon we convene the committee's second hearing on trade and competitiveness issues. Yesterday, we heard from a number of small business experts and international economists on the competitive problems and opportunities confronting our small business sector.

In today's hearing, we will receive testimony from the Federal agencies that have direct contributions to make to the competitive prospects of this important part of our economy.

We know that the potential for small- and mid-sized companies to contribute to the growth of our economy depends, in large part, on their ability to be competitive in international markets. We hope that these hearings will help us to formulate some useful initiatives for inclusion in the House omnibus trade bill.

We are pleased to have with us, Mr. Bruce Smart, Under Secretary for International Trade, U.S. Department of Commerce and Mr. John Bohn, the president and chairman of the Export-Import Bank.

From the Small Business Administration, we have Frank Swain, Chief Counsel for Advocacy, Mr. Richard J. Shane, Assistant Administrator for Innovation, Research, and Technology, Mr. Edwin T. Holloway, Associate Administrator for Finance and Investment, Mr. John Cox, Acting Associate Administrator for Management and Administration, Mr. Michael E. Deegan, Director, Office of International Trade, and Johnnie Albertson, Deputy Associate Administrator, Small Business Development Centers.

We will not be hearing testimony from every representative from the SBA, but we understand a good many of them are here to help answer questions as we proceed.

Because of time constraints, certainly on my part, I am going to ask unanimous consent that we introduce the prepared text of everyone before us who has a prepared text in the body of the record, and then we ask all witnesses to please give a verbal presentation or summary in no more than 5 minutes apiece.

Are there any objections?

Hearing none, so ordered.

Before we proceed to the panelists, however, does any member of the committee have any statement they would like to make?

Well, with that, let us begin.

Mr. Smart.

TESTIMONY OF BRUCE SMART, UNDER SECRETARY FOR INTERNATIONAL TRADE, U.S. DEPARTMENT OF COMMERCE

Mr. SMART. Mr. Chairman, thank you for the chance to appear. I was doing a little quick editing to get to 5 minutes. I will do my best. I would like to make a brief statement.

Chairman LAFALCE. Sure.

Mr. SMART. I have spent 36 years as a business executive, and during that time I have been fascinated by the web of enterprise that constitutes the American economy, and how firms of all sizes have fitted together to create the standard of living and the industrial preeminence that we enjoy, and frankly, that I am afraid we are taking for granted as an entitlement.

That preeminence is in danger of being lost, and to protect it we need to awaken America to the need to compete, to adapt, and to win, both at home and on the road. I welcome your hearing as a step in that direction.

Obviously, smaller businesses need to play a key role in our competitiveness effort. Typically, small firms represent sectors such as new market entrance, specialized manufacturing that can be conducted efficiently on a small scale, services, suppliers of components and parts, and marketing and distribution organizations.

Those businesses will flourish in a growing and vibrant economy and not be well served by one that is static. So our initiatives to improve overall U.S. competitiveness will benefit small companies directly. They will also benefit directly in their role as suppliers to large businesses. Our trade statistics do not capture this role of small firms as invisible exporters, but they do have great potential also as direct exporters, and Government can help them to be more effective in foreign markets.

Some of the problems that we find small business facing are inadequate market knowledge, limited access to overseas business connections, the high costs associated with entering a foreign market, inadequate financial resources, and problems of market access. The President's competitiveness initiative addresses a lot of these problems.

Often small businesses do not have resources to develop international marketing information. We are proposing an export promotion data system which can help them overcome this. The Export Trading Company Act can be helpful as well, and we are proposing improvements to that. Competitive financing is always a concern. I think my friend John Bohn will have some comments on the Eximbank role in that area.

Product liability has been identified by the White House Conference on Small Business as their top concern. The administration is proposing some reforms in that area. The Foreign Corrupt Practices Act appears to be a concern of small business as they attempt to find their way through that law without engaging in bribery which some other countries practice. The export control system is a particular concern, and we have made an 11-point program, some of which will require legislation to improve the efficiency with which we both control national security and assure long-term vitality. Small businesses particularly have been impacted by the shortcomings of that particular activity.

Small businesses have much to gain from a better, more disciplined, and more comprehensive world trading system. The Uruguay Round was launched last fall. It will include services, intellectual property, and investment disciplines not now present in the world trading system, all of which should make it easier for small businesses to take a bigger place in international trade.

We have been very active in my International Trade Administration in export promotion. Many of the companies that we serve in that respect are small businesses that do not have the resources to go it alone without Government help. We include, in our efforts, outreach programs to make them aware of export possibilities. We offer counseling and how-to publications and custom-tailored market information. And we conduct trade promotion events here and abroad to call export opportunities to their attention and to call them to the attention of foreign buyers. We work closely in this respect with the Small Business Administation, the National Governors' Association, State development agencies, and the USIA.

I think it is important, though, to realize that in discussing the special needs of small businesses, we cannot somehow assume that they can be entirely segregated from larger businesses or that they are in some way more virtuous or meritorious than their larger competitors. America needs all parts of its economic machine to operate at full throttle. Each part depends on the others for success. A small spark plug is useless if it has no fuel to ignite or a large engine to drive, nor can the large engine produce without the stimulus of the spark plug.

But small companies do have special needs, and I believe it is the responsibility of Government to understand those needs and to work for a business climate in which an aggressive and innovative small business can be successful.

Thank you.

[Mr. Smart's prepared statement may be found in the appendix.]

Chairman LaFalce. Thank you very much, Mr. Smart.

Our next witness will be Mr. Bohn of the Export-Import Bank.

TESTIMONY OF JOHN A. BOHN, JR., PRESIDENT AND CHAIRMAN, EXPORT-IMPORT BANK

Mr. Bohn. Thank you, Mr. Chairman.

What I would like to do is summarize, as quickly as I can, the various issues that I think are of concern and of interest to the committee.

Since 1983, with the legislation enacted at that time which mandated us to push in the area of small business, and with the addition of the legislation in 1986, I believe we have all of the legislative impetus we need. In each of the previous 3 years we have more than reached our mandated small business set-aside. In fiscal 1986, 23.7 percent of our authorizations went for small business; that is to say, $1.4 billion out of a total of $6.08 billion authorized was used for small business exports.

Virtually all of our marketing efforts—we have a separate marketing department devoted principally to small business—have been devoted to increasing the awareness of small businesses of the Export-Import Bank programs. In 1986, for example, we made presentations to some 5,000 people in 36 States related in large part, if not by far the majority, to the small business area.

Rather than go into more detail, Mr. Chairman, I would call the committee's attention to our 1985 annual report. All of the pictures on the cover of the annual report relate to small businesses that we have supported, and their stories are inside here, and I will be happy to make that available to the committee.

Again, rather than read a typical letter of the kinds of things we have been able to do for small business, I have one letter dated October 3, 1986, from Victor Jurnigen, who has been a very successful user of our programs. I would be happy to make that available as well.

One other item—we have been trying our very best to re-invigorate banks' interest in supporting small business, and I would again offer the committee a copy of an ad put forward by the BayBanks of Boston which deals with the working relationship between themselves and a small company using Eximbank programs. I will just read one quote here:

It says, "My banker knows what color socks I'm wearing and exactly what's going on in my business. For the first time in my banking relationships I'm content."

And this dealt with a series of transactions that the bank did using our programs.

We have certified almost 300 banks since the Certification Program began, and we have trained many Department of Commerce people, as well as SBA people and others, in our specific programs. The greatest interest for the small business so far, in terms of the new programs, has been the Working Capital Guarantee Program. We have done 104 cases since that began, for a total of $110 million committed and $56 million has been drawn down. There have been 75 exporters using 63 banks in 26 States, and these exports have gone forward to 27 countries. This is one of the cases, Mr. Chairman, where the program, at least on a cash-in-cash-out basis, is slightly ahead of break even.

Typically, it deals with lumber, machine tools, and educational equipment. The smallest case was a $25,000 case we did under the delegated authority in Minnesota. We have a program of delegated authority to the banks to attempt to encourage the banks to work more actively with small business. They have done 16 transactions so far, involving roughly $13 million.

As you know, we have worked actively with the SBA to reinsure and improve their capacity to deal on the international side in this program, which I think began in 1984. Since that time, we have done six transactions with them amounting to $3.6 million.

The important thing, Mr. Chairman, on the Working Capital Program is that it provides, for the small company, the ability to go to his or her local bank and obtain financing for a particular export opportunity. We found that the program, unfortunately, was slower in starting than we had thought, but the volume, I think, in 1987 so far will equal all of 1986, and we expect that kind of increase to continue.

We have designed our New-to-Export Program with lower premiums, and we provided a hold harmless agreement to the banks in order to compensate for the expected inexperience in many cases of the small companies.

In the small business credit program, which we initiated as well, we do not require a showing of foreign competition, and under the legislation enacted in 1986, a company that cannot find a bank to support their transaction may now come directly to us.

FCIA in general is the most active engine that we use to support small business. Most of the small businesses find the insurance program more effective and more efficient for their use. In 1986, for example, the special small business underwriting unit at FCIA underwrote some 1,000 buyer and exporter transactions.

Again, in this program, we provide a 30-percent discount for a small business from our normal fee schedule, and I also have to say that in January of this year we introduced a single sale policy, which has been a matter of great concern, particularly, for the small- and medium-size exporters for a long time.

I have to say, Mr. Chairman, one of the concerns of the small businessman typically is the complexity of dealing with the Government, certainly in our area, but I would show you a one-page sheet to complete on both sides which constitutes the entirety of the single-buyer export credit insurance policy. We think this is the beginning of some important simplification steps which will benefit the small businessman.

In addition, we have tried a first in providing an umbrella-type policy for a trade association, namely, the National Machine Tool Builders Association. The theory here is that a machine tool builders association or another trade association, acting on behalf of a number of its members, will be able to provide much of the secretariat-type work, much of the expertise, which would not be cost-effective for a single company. It also provides some marketing leverage with a bank, and the Machine Tool Builders Association has negotiated with a particular bank to handle all of the trade finance needs of the membership under this policy.

We are watching this very carefully because we think that the intermediation process provided by this will be a very important prototype for other trade associations and other cooperative groups.

There are two problems, in summary, Mr. Chairman, that we have tried to address with our new programs announced earlier this month. One is access. A small business person typically does not have access to us in Washington. It is essential that they have access through some intermediary, whether it be a bank or a State agency or a trade association. What we have found, as a result of some extensive studies, is that the banks have simply been unwilling in many areas to provide service for the small business person——

Chairman LAFALCE. Could I interrupt you, Mr. Bohn——

Mr. BOHN. Sure.

Chairman LAFALCE [continuing]. Right now, because I think this is extremely important. I have generally approved of the conduct of the Eximbank under your leadership, although the resources you have to work with are minuscule in comparison. You should have $5 billion rather than $1 billion, particularly if we are going to be making a dent in our trade deficit. Eximbank should help lead the way, not be extinguished.

But you do not have a very effective—this is not your fault—you do not have an effective delivery system. And that is basically what you are saying right now. And you need some intermediary.

Now, you have just named a number of potential intermediaries, private financial institutions, you suggested. I forgot what else you suggested.

Mr. BOHN. State agencies.

Chairman LAFALCE. State agencies.

Mr. BOHN. Trade associations.

Chairman LAFALCE. Trade associations, and I think you are trying to work out a deal with the National Machine Tool Builders Association.

Mr. BOHN. Yes; we have done that, and we are watching that with great interest.

Chairman LAFALCE. Well, I am going to watch it with great interest, too. If you can use the State agencies, then why not a Federal agency? Why not the SBA, which has a tremendous service capacity right now. They have field offices all over the United States. Why not the SBDC Program, which is existent in, I think, 48 of the 50 States. Why could they not be the packagers of Eximbank's programmatic capacities?

Mr. BOHN. Well, Mr. Chairman, we would be delighted to support either or both of those suggestions. As you know——

Chairman LAFALCE. Great. You have got a deal.

Mr. BOHN [continuing]. About 2 years ago, maybe 3 years ago now, we entered into an agreement with the SBA whereby we would support them in this working capital area, which is a matter of great interest for the small businessman engaged in exports.

It has been somewhat disappointing that we have not had more activity there, but it is quite understandable. The reason for it is that the Working Capital Program, which relates strictly to the domestic financing side, is a fairly complicated loan to make.

We have invited a number of Small Business Administration people to our seminars to learn about our programs. We are delighted to train as many of them as we can, and frankly, you put your finger on the principal problem as I see it, namely, the delivery system.

Chairman LAFALCE. Could we come up with a program where, whenever SBA is having its in-service training for its employees, Eximbank could provide its personnel to educate SBA not just about Eximbank's programs, pursuant to the thought that after this training period, the SBA finance people, for example, could prepare the applications and possibly even approve the applications. Now, you might want to retain approval authority, but at least the explanation of your programs, the assistance on the application preparation, the submission could be processed through a local SBA office for Eximbank.

Mr. BOHN. We would be delighted.

Chairman LAFALCE. Oh, great. Let us stop while we are ahead.

Mr. BOHN. There is a second dimension to that, Mr. Chairman, which I think is probably equally important, and that is we have worked with SBA, and the Department of Commerce as well, to try to create a national awareness down to the local level of the fact that these programs do in fact exist, how they work, and all the rest of it. I would like to suggest that as part of this process that we are talking about, we might be able to help and work with the SBA to actually publicize what some of these programs are all about.

Our principal concern in many areas is that the small businessperson simply does not know the programs exist and therefore does not ask.

Chairman LAFALCE. Sure. Well, how many seminars can you put on with the small business community? I do not know if you have been able to put one on in every Member of Congress' district, and you put one on in my district about 2 years or so ago, and there were *x* number of people who attended it, but you did not begin to penetrate the potential small business market.

Mr. BOHN. No; and we really cannot.

Chairman LAFALCE. And, of course, you cannot. But if others are knowledgeable and in these countless seminars that are conducted by the SBA—or the Department of Commerce, or the Department of Defense—a component could include the Eximbank capabilities, then it would seem to me we would be helping the small businessman to have access to that international market.

Please continue. I am going to have to leave at around 1:45, and then I am going to turn the hearing over to Mr. Olin to chair.

Mr. OLIN. Thank you.

Chairman LAFALCE. Thank you. Usually I like to give other members the chance to ask questions first, but I will try to get in my questions as we go along.

Are you finished, Mr. Bohn?

Mr. BOHN. Yes; the only other point I would make, Mr. Chairman, is that, as you know, we have Mr. Simon Fireman who has recently joined our board of directors, and is designated as the small business director. He has re-initiated a series of discussions with the Commerce Department, and with SBA, along the lines to which you refer. They have had two meetings already and a third is scheduled. I am sorry he cannot be here today; he is ill in Massachusetts with pneumonia at this point, but his basic focus is to deal with the small business problem.

Chairman LAFALCE. Great. Before I leave you, though, did you get a chance to look at the bill that I got through subcommittee Tuesday with respect to Eximbank?

Mr. BOHN. Yes; very quickly, Mr. Chairman.

Chairman LAFALCE. And your general thoughts? We just basically called for a study on your part, as opposed to actually changing your charter.

You want to wait until you study it?

Mr. BOHN. Well, Mr. Chairman, again, I read it very quickly. I think that the issues that you focus on there are very definitely issues that need to be dealt with, and we will be prepared to do our very best to come up with the kind of analysis that will be useful.

Chairman LAFALCE. Terrific.

[Mr. Bohn's prepared statement, with attachments, may be found in the appendix.]

Chairman LAFALCE. Mr. Swain.

TESTIMONY OF FRANK S. SWAIN, CHIEF COUNSEL FOR ADVOCACY, U.S. SMALL BUSINESS ADMINISTRATION

Mr. SWAIN. Thank you very much, Mr. Chairman.

It is an honor to appear before the committee, and I congratulate the committee and you, sir, for convening this important set of hearings.

Small businesses do have an important stake in the outcome of policy discussions in the international trade area. Certainly, our national ability to increase our economic competitiveness on an international scale depends on continued growth of the small business sector. Policies that expand small business opportunity build on the strength, and policies that protect us from change are policies that hurt small business.

We believe that most small firms are affected by international competition. They may well be, knowing or unknowing vendors of imported products, or manufacturers, or suppliers, or distributors of products that are destined for export. We believe our competitiveness policy must address not only import and export policies, but also those impediments to competitiveness in the form of domestic policies that we impose on ourselves. We think the long-term success of small business depends on our ability to tackle these regulatory and legal burdens.

I think the role of small firms is particularly illustrated by several areas where—which we cite in our testimony—small business growth has, to a degree, offset losses in jobs in large, and even to a degree offset losses that might be directly traceable to allegations of foreign competition. Certainly the experience in the steel industry, which has been undergoing, as the chairman knows so well, a very painful restructuring, does give us some cause for hope. While large firms were not doing very well, small steel manufacturers grew by 39 percent. These specialized mills are not only supplying and in some cases competing with U.S. firms, but they are in many cases competing quite successfully with foreign firms, and we would like, obviously, to see this become a model for several other industrial sectors in the economy.

The question that the committee is clearly interested in is what policies should Congress address to ensure that small firms increase their contribution to the flexibility of the U.S. economy. In dealing with small businessowners, through the White House Conference on Small Business, I think it is very fair to say that overwhelmingly small businessowners, men and women, are, by and large, free traders. Now, certainly, that is not always the case. If you go to Maine and ask shoe people what their perception is, they may not claim to be free traders, nor are auto parts manufacturers in Wisconsin, necessarily. But by and large, the general consensus is small firms are free traders. They realize that import barriers that are erected this year may come back to haunt them in years to come.

So, I think that there is a general consensus in favor of as open and free competition as possible, and I would certainly add to Under Secretary Smart's assertion of the importance of the Uruguay Round of GATT, and in particular as it has been extended to include service negotiations for the first time.

I might also add that we are pleased that we are currently working with the Special Trade Representative's office in advising them on bilateral negotiations with Canada insofar as the impact on small firms, and we anticipate, in fact, having a meeting on that particular subject with businessowners in Buffalo next week.

Second, the White House Conference did endorse a single Federal agency for international trade policy. I am not really sure the delegates to the conference were so much concerned with the way the bureaucratic boxes were arrayed in the sense of whether there is a single agency or more than one agency, but I do think that they expressed a clarion call for better coordination among Federal agencies and among Federal, State, local, and private sources of export assistance. Certainly the many steps underway at the Commerce Department and at the Export-Import Bank as already outlined by Mr. Smart and Mr. Bohn are certainly steps in the right direction, and we certainly hope that we will hold up our end of the responsibilities at the Small Business Administration. We would certainly endorse in general the suggestions for further cross-training that your questions implied.

Finally, delegates to the White House Conference identified and called for action on several, what are in effect, domestic barriers to further competitiveness, whether it is reform of the tort laws or concern about the Government mandating various employee benefit policies, Federal deficit, Davis-Bacon Act, and many others.

We think that this is vitally important. Today, total exports and imports represent about 20 percent of our gross national product. By the year 2000, this figure will represent more than 30 percent. We are in an international economy, and we are going to be more so rather than less so as the years go on. The small business community has a strong stake in whatever the Federal policies and programs are, and we feel that the Congress has to take a several-pronged approach, looking not only at the international issues, but looking at the domestic issues.

I would be happy to respond to any questions.

[Mr. Swain's prepared statement may be found in the appendix.]

Chairman LaFalce. Thank you, Mr. Swain.

Maybe I should not ask this of you; maybe I should ask it of others. But does SBA have an export financing program?

Mr. Swain. Yes, sir.

Chairman LaFalce. And it is my understanding it has been very poorly utilized. I am told that seven loans were given in 1 year, and absolutely none the next year under their special Export Financing Program. Is that accurate, and if it is accurate, why is that the case?

Mr. SWAIN. It is partially accurate, Mr. Chairman, and I think I am going to have to defer to Mr. Holloway on the exact figures.

I think the figures that you have, relate to the joint program that we have with the Export-Import Bank, and those figures are accurate for joint programs. I think that in addition to that there have been some number of loans that we have made on our own under the SBA Exported Credit Program, although I am not going to sit here and say that it has been a very substantial number.

Mr. Holloway could certainly tell you specifically.

Mr. HOLLOWAY. Mr. Chairman, the Small Business Administration has had roughly $20.5 million since 1983.

Chairman LAFALCE. 1983 through 1986. Let us say 4 years, roughly 20 loans a year.

Mr. HOLLOWAY. That is correct, Mr. Chairman. And as you know, the SBA——

Chairman LAFALCE. Roughly $5 million in loans per year. That is pretty pitiful. That is pretty small, is it not? Those are guaranteed loans, are they not? As opposed to direct?

Mr. HOLLOWAY. Yes; they are all guaranteed loans.

Chairman LAFALCE. Why such a small amount?

Mr. HOLLOWAY. I just want to point out that where the private sector, that is the banking community, ordinarily is accommodating to credit need, they do not come to the SBA with it.

Chairman LAFALCE. So we give out such a small number and small amount because the private financial institutions are taking care of it all by themselves.

Mr. HOLLOWAY. I think on short-term lending they are accommodating most of it, Mr. Chairman.

Chairman LAFALCE. Why do we need so much more money through Eximbank? Why do we need an outreach program through Eximbank? Why do we need a better delivery system then, if you say the reason we have so few financing exports through SBA is because the private sector is taking care of it.

Mr. HOLLOWAY. I am attempting to address the issue of the very short-term working capital free export expenses that are ordinarily associated with this program. Banks do a pretty good job on the short-term lending. And the particular niche of SBA is long-term lending. That does explain to some extent the small amount of activity under this program.

Mr. SWAIN. Mr. Chairman, let me suggest a couple of reasons. First of all, I think it is clear that the program has probably not been utilized to the degree that the Congress expected when it granted the SBA authority to do it, and certainly to the degree that we expected to do it when we executed the memorandum of understanding with Eximbank 3 years ago. I think there is a combination of reasons, which I am not making as an excuse but simply to explain my perception on it.

First are some macro reasons. With the high dollar the demand for exporting has not been as big as we would have liked. Second, the reasons that Mr. Holloway indicated is that the SBA and our vast field organization has experience primarily with long-term lending. The short-term line of credit is something that our people are just not familiar with. And third, our people have not been, heretofore up to the start of this program, very extensively involved in export financing at all. And so in many cases their client banks, which tend to be the small- to medium-sized banks, are very much different than the client banks in Mr. Bohn's organization. That is why I strongly agree with his statement, that the real challenge is the intermediaries, both in the technical sense of the word, financial intermediaries, and getting more banks willing to finance small business exports. And in the more general sense of the word, getting more people to go out and do missionary work about why small businesses ought to export.

Chairman LAFALCE. Is there anything we can do, either within legislation or within regulations to so improve the SBA financing programs that the small businessman would be able to make better use of them? For example, right now you have an 18-month limit, do you not?

Mr. SWAIN. Yes sir.

Chairman LAFALCE. Should it be an 18-month limit? Is that a problem? Should that limit be increased? Is there anything else that we have that might be an impediment to the use of that program that could be changed, either by regulation or by statute?

Mr. SWAIN. We are actually able, under the 7(a) General Business Loan Program, to go up to 25 years for fixed asset financing and that type of thing. So we can accommodate those long-term needs under the General Business Loan Program.

Chairman LAFALCE. What is this special program you have that has an 18-month limit?

Mr. SWAIN. The special program is the revolving line of credit. For example, if you want to ship the Christmas toys now and you will be paid within 3 months, you need some short-term money.

Chairman LAFALCE. Do we need a longer period for the revolving line of credit?

Mr. SWAIN. I do not believe we do, Mr. Chairman.

Chairman LAFALCE. Is there anything other than a macroeconomic reason why it has not been used very much?

Mr. SWAIN. I think the awareness on the part of small and large businesses as to the potential of the overseas exporting markets is the important thing. If that awareness is there and there is an interest in shipping overseas, the financing through the banking community and the Government, where necessary, will also be there.

Chairman LAFALCE. Few people are aware of that.

Mr. SWAIN. Mr. Smart alluded to this in his statement as well. There are two problems. One is generally getting small American firms who have the potential to export because they make a quality product that somehow there is a market for in some other part of the world, it is getting them to realize that and using all of the excellent avenues at the Department of Commerce to find out how they develop those markets overseas.

The second subsidiary issue is, once the businessowner makes that decision, then how do they go about getting financing? How do they approach the Eximbank or the SBA? And I am not sure that solving that problem of awareness is something that can be legislated. It is an evolving process. I dare say there are a lot more small firms aware of exporting now than there were 10 years ago, but probably very little of that has to do with legislation through Federal programs.

Chairman LAFALCE. Mr. Shane, did you have some comments that you were going to make?

TESTIMONY OF RICHARD J. SHANE, ASSISTANT ADMINISTRATOR, OFFICE OF INNOVATION, RESEARCH & TECHNOLOGY, U.S. SMALL BUSINESS ADMINISTRATION

Mr. SHANE. Mr. Chairman and members of the committee, it is a pleasure to appear before you and the committee today to express the Administration's thoughts in regard to the Small Business Innovation Development Act of 1982 and its pertinence to the country's trade and competitive position.

At the outset I would like to express the Administration's and my personal appreciation for the continuing interest and support of the chairman and the committee. The achievements of the Small Business Innovation and Research Program are gratifying in that it is meeting or exceeding the purposes of the legislation.

This success is due to the mutual efforts of the administration, the Small Business Administration, the participating agencies, and the committee. I would like to make note of the fact that the chairman has continued his personal support of the program since its inception.

On June 17, 1982, the chairman, acting as floor manager, presented to the whole House of Representatives H.R. 4326, the Small Business Innovation Development Act. At that time he stated, "We cannot afford to lose our ability to innovate. If we lose that, we lose our ability to increase U.S. productivity, we lose our ability to maintain U.S. technology and technological preeminence, we lose our ability to create many of the 20 million new jobs essential for a full employment recovery. We lose our ability to compete in the world markets and we lose our ability to prevent permanent damage to our economy and society."

[Mr. Shane's prepared statement, with attachment, may be found in the appendix.]

Chairman LAFALCE. Mr. Shane, I am going to stop you there. What can we do to improve the SBIR Program in order to enhance exports, and in order to help reduce our deficit?

We had some suggestions yesterday from Milt Stewart, who I worked with closely when we created the SBIR Program, statutorily. We had some suggestions from Mr. Johnson, I think, and Mr. Little, too. Mr. Swain in his testimony mentions the recommendation of the White House Conference for an Export SBIR Program. I think you mentioned that, did you not Mr. Swain?

Mr. SWAIN. Yes; I did.

Chairman LAFALCE. Mr. Swain, what did you mean by an Export SBIR Program? And Mr. Shane, what thoughts do you have for either expanding the present SBIR Program or modifying it before expanding it, or creating a new type of program modeled on the SBIR for the purpose of enhancing exports? Mr. Swain first.

Mr. SWAIN. Mr. Chairman, the concept of Export SBIR is one that was introduced as a resolution in the White House Conference for Small Business. What it generally refers to is that the approach of the current SBIR Program in collecting a series of accounts around the Government which are called R&D, for purposes of Mr. Shane's program, and saying that a certain percentage of those moneys should be earmarked for a competitive program among small firms.

There has been a suggestion that a similar sort of program be tried in the international trade area; that various Federal programs in a variety of agencies, and there are many programs and agencies beyond those that are represented here, be collected in effect, and a certain percentage of each of those accounts be targeted for small firms. Beyond that I cannot get into specifics because it is a very general concept. And in fact, we are about to authorize a research program to try to sketch out this kind of concept more specificially.

Chairman LAFALCE. You are envisioning this within the present set-asides for the SBIR Program, are you not? Or is that separate?

Mr. SWAIN. No; I do not think the SBIR refers to having an addition to Mr. Shane's program per se, but to use an SBIR approach to collecting a variety of accounts from around the Federal Government, in this case moneys that are dedicated somehow to export promotion.

Chairman LAFALCE. So you are talking about export promotion as opposed to procurement.

Mr. SWAIN. Yes sir.

Chairman LAFALCE. And setting aside a certain amount of those moneys.

Mr. SWAIN. And presumably, but I am not quite sure because the concept is a little bit vague in the White House Conference, but presumably small firms would in effect compete with their marketing ideas, or whatever, to have certain awards within those accounts.

Chairman LAFALCE. That was one of the approaches suggested yesterday. There are other approaches too. Maybe we should try all of the different approaches. I do not know. Although you run into different opposition constituencies depending on the approach that you are going to take.

Mr. Shane?

Mr. SHANE. We have taken a look at this recommendation since the White House Conference. I think it is a dichotomy or at least a mixture of terms, the SBIR Program and an export program. I do not think they really come together, one being a national R&D procurement program, one being a marketing and production program for overseas sales.

What I see in viewing it from the outside, if you will, is that the basis of the success of the SBIR Program was drawing together under one agency the authority and responsibility to direct a program through multiple agencies and this is rarely done in the Federal Government. This gave the SBA a directed amount of responsibility and authority that we would not normally have.

Second, we were given a gift from Congress in allowing us to simplify the acquisition system for the SBIR program. I have heard no one so far explain what are the problems of exporting. I must assume there are a lot of problems, there is a lack of information, there are a lot of barriers, and there are a lot of things that could be changed to simplify the process. Where it has a likeness to the SBIR Program is that we had to inform the public of the program. In the first year of the program we sent out over 1 million pieces of literature, spoke at 85 conferences around the country, and were on public radio almost 300 times. This was necessary to generate and produce a new direction.

To bring the export programs to a new level or design, one would also have to move into a mode of outreach. I think we had a difficult time in the beginning to inform people of our intent. This was not an easy task.

Chairman LaFalce. Very good. Mr. Smart, what does the Department of Commerce have programmatically for the small business community insofar as outreach to the small business community?

Mr. Smart. Mr. Chairman, we cover it reasonably fully in our prepared testimony. We start with offices in 50, or thereabouts, cities around the country. Most of those district offices have export councils made up of experienced private businessmen engaged in export. Through those we reach to companies in the area of the offices' responsibility to identify a perspective new-to-export company to determine their capabilities for engaging in export and the acceptability of their product in an export market.

And we put them together through our sister foreign commercial service with opportunities in foreign countries where the buyers of their wares exist. We use that network to help individual companies who wish to go overseas, calling attention to things such as the Eximbank support. We put on trade shows that are related either by nation or by industry as well. And we support buying missions that come to the United States wishing to get in touch with companies that might supply what the buying mission wishes.

For example, we will be working very closely with an auto parts seminar put on by the Japanese industry and us in conjunction with the state of Indiana in May of this year.

Chairman LaFalce. An auto parts seminar put on by the Japanese?

Mr. Smart. Put on and supported by the Japanese, by the State of Indiana, and by ourselves.

Chairman LaFalce. Let me just take a moment to discuss that subject. Everybody talks about the auto parts industry, and I think we ought to be focusing special attention on the auto parts industry, which is in large part made up of the small business community.

Mr. Smart. Many small companies are involved.

Chairman LaFalce. Many, many small companies. And I think the auto parts industry is becoming an endangered species within this country. The auto parts industry has lost about 400,000 jobs in about the past half dozen years. And by the end of this decade, I am fearful we are going to be losing about 200,000 more.

When I hear the Japanese are having a seminar——

Mr. Smart. No, no, no.

Chairman LaFalce. Let me just finish my thoughts. The embassy in Tokyo just came out with a report. I think it is called the Heuristic Report, in which they said approximately 300 Japanese companies are poised to come here to the United States. It sounds as if it is good—we are going to get new investment here. But virtually all the parts that are being put under the hoods of Japanese cars, maybe about 70 percent, are being supplied from Japan rather than domestically, even though the cars are assembled here.

Right now, American cars have about 30 percent of their parts from abroad, even though they are American cars made here. I think by the end of this decade, it is projected that 50 percent of the contents under the hood of a Big-3 car will be from abroad. And I am fearful that pretty soon about the only thing American about these cars is going to be the name.

I know the MOSS negotiations are underway right now. Are you actively involved with the USTR's office in the MOSS negotiations with respect to the auto parts industry?

Mr. SMART. Mr. Chairman, I am the vice minister level, if that is the right word, leader of the United States side in those MOSS negotiations.

Chairman LAFALCE. How is it that the Department of Commerce is a leader, as opposed to USTR?

Mr. SMART. First of all, the whole auto parts subject came up under the auspices under the U.S. Department of Commerce, our Trade Development unit, and Assistant Secretary Goldfield. We brought it to the attention of the MOSS process, which comes into the U.S. Government through the State Department, and recommended and were successful in having the Japanese agree that it should be given the MOSS imprimatur.

That is a rather unusual thing because the problem in the auto parts industry is not a government-to-government or a government barrier problem. It is the practices of private businesses in Japan and how they buy.

Chairman LAFALCE. They only buy from their brother or sister companies—the Nissan family.

Mr. SMART. Exactly.

Chairman LAFALCE. But they are coming over. They are going to be supplying parts to the Big-3.

Mr. SMART. Mr. Chairman, I am fully aware of that. This is the reason that——

Chairman LAFALCE. To get to the bottom line, are we going to try to do what the United Kingdom did? Negotiate a certain percentage of domestic content when it comes to parts?

Mr. SMART. No sir.

Chairman LAFALCE. The United Kingdom negotiated what—80 percent?

Mr. SMART. How is their auto industry doing sir?

Chairman LAFALCE. The only way our auto industry is doing well is because we had protectionism for 4 years because of the voluntary restraints. If we did not have that protectionism for 4 years, our auto industry would probably be kaput. And now I am worried about our auto parts industry. There are different forms of protectionism.

Generally, I am opposed to the concept of protectionism, except that things would get so bad that you are faced with extinction. And I think that in the auto parts industry, things are getting so bad right now that we are faced with extinction. What are your plans?

Mr. **Smart**. Basically, what we have done is, we have got the MOSS imprimatur on these talks. That means that we have enlisted the support of the Japanese Government in urging Japanese auto companies to broaden their horizons as far as their prospective suppliers. Our ultimate target is to break down the practice of kiretsu, which is what you described as buying from your brother-in-law. And that is exactly right.

And we do that by getting our companies accepted by Japanese design and engineering departments in Japan as qualified suppliers for Japanese brand automobiles. The first place you have to do that is in those engineering departments in Japan. But the best volume you will get is with the Japanese brand automobiles assembled in the United States because United States suppliers can clearly find it more easy to serve this market than to serve the Japanese market.

We hope though to increase our sales not only here, but in Japan, in third country markets where the Japanese also build cars, and not only for the original equipment sales but for the after-market sales for repair parts.

How successful are we going to be? I cannot say. I do know that every time now that we have a meeting with any Japanese auto company, they are very quick to point out what their targets are for buying increased quantities of United States parts and materials for their plants in the United States. They have all identified focal points for purchasing within their companies that our companies can go to.

We have addressed complaints with them, both complaints that we have about lack of access of our companies into their companies and complaints that they have, whether real or imagined, about our ability to supply quality service and prompt delivery. And by continuing to pound on this we hope to improve our line.

Chairman **LaFalce**. I thank you for that. I have a million questions on that specific subject, and we will be having a special hearing strictly on the subject of the auto parts industry. We will want to go into the specific problems that we have, problems posed by the Japanese, problems posed by our own auto parts industry, problems posed by Federal laws, for example, foreign trade zones. Problems posed by perhaps the Maquiladora Program. Problems posed by unbelievable State subsidies of foreign investment, bringing about tremendous dislocation. I think it will be an interesting hearing.

I am not sure exactly what we should be doing. But I just know that we had better do something because pretty soon it will be too late. I am pleased that the MOSS talks seem to be taking a much more aggressive stance in the past 6 months or so on this issue. This is something, I think, Congress should be much more involved in and the Small Business Committee also.

I also want to apologize to the panelists and to the members of the committee for the fact that I have to leave now. Usually I like to defer my questions until the end, but because I have to depart, I tried to get in just a few of them.

I do want to keep the record open so that we can submit written questions to every panelist and have you respond to us in writing.

At this time, I would like to ask Representative Olin to assume the Chair.

Mr. OLIN [acting chairman]. Well, let us see if we can see where we are with the testimony. Mr. John Cox.

TESTIMONY OF JOHN R. COX, ACTING ASSOCIATE DEPUTY ADMINISTRATOR FOR SPECIAL PROGRAMS, U.S. SMALL BUSINESS ADMINISTRATION

Mr. COX. Thank you, Mr. Chairman.

Mr. Chairman and members of this committee, I appreciate the opportunity to appear before the Small Business Committee today to discuss the Small Business Administration's efforts to assist small business in the international trade area. The Office of International Trade was legislatively established in Section 3 of Public Law 96-481. Through a staff in Washington, regional international trade offices in our 10 regional offices, and designated persons in our district offices, we are working within the international trade network of Federal, State, and local private and public sector organizations to help broaden the Nation's base of successful small business exporters.

This committee, Mr. Chairman, has noted in various reports that small firms are very often reluctant to explore foreign markets as a source of additional sales. The reluctance stems from not knowing where to find which companies who may want to buy their products and other services they produce. They do not know how to go about obtaining assistance or consolidating the vast amount of information that is actually available.

In surveys conducted by the SBA and the National Federation of Independent Business, the Senate Small Business Committee, the Chamber of Commerce of the United States, and other organizations indicated a lack of information on, one, where markets exist for their products and services, and, two, the procedures to be followed in successfully competing potential sales within these markets.

We recognize that there are many organizations within the public and private sectors that are involved in international trade. We share the same objectives, to increase the competitive position of American business in the world marketplace. By working together in this effort, the small business community will grow and prosper, create more jobs, and foster innovation which has been the hallmark of the American free enterprise system.

We are encouraging our district offices to become members of local world trade organizations and the Department of Commerce district export councils, in order to become aware of and participate in their activities where appropriate. Our district offices have been instructed to have available local directories of export assistance programs and services. During fiscal year 1987, we will be increasing our efforts on greater outreach to the small business community.

Our procurement automated source system, known as PASS, has identified over 50,000 small business firms that have an interest in exporting. We will be reaching out to these firms, making them aware of the various services available to them, under export counseling, basic counseling concerns, how to identify markets and establish and conduct export operations, is offered by our service corps of retired executives, known as SCORE, and the active corps of executives, known as ACE.

Each SBA district office and SCORE chapter is dedicated to recruiting additional counselors and developing counseling teams as needed to initially contact potential small exporters and provide them with basic counseling and training. More in-depth market research and assistance is available through the Small Business Institute's university-based system. International trade counseling is also available through small business development centers.

Our export information system, known as XIS, is designed to answer the basic question, a question on how a would-be exporter would ask, where might there be a market overseas for the products similar to mine. Under an agreement between the Small Business Administration and the Federal Bar Association [FBA], a small firm now can receive an initial free consultation with an attorney to discuss legal issues and concerns relating to international trade.

During fiscal year 1986, export-import counseling was provided through these resources to over 3,500 clients. Under export training, district offices of the Small Business Administration cosponsor export training seminars and workshops; training programs are also conducted by SCORE and ACE volunteers, small business development centers, and other universities and junior colleges, as well as private sector entities.

In fiscal year 1986, 419 such programs, attended by over 17,000 persons, were held. In fiscal year 1987, we intend to become more involved with private sector organizations, including for-profit corporations, as well as Federal, State, and local governments, in supporting outreach programs such as conferences, seminars, and workshops which identify potential small business exports and provide linkages to needed information and assistance.

Beginning in the fall of 1982 through June 1986, SBA agreed to support the participation of 241 small businesses in 30 export promotional events, such as trade shows and trade missions. These shows and missions have taken place primarily in the developed countries of Europe and the Pacific rim. These events have been beneficial to those businesses that participated. However, this type of activity has had minimal impact when considering the scope of assistance that is needed by the small business community in the international trade area. In addition, trade mission support is being provided by private sector, and we feel that we can better serve the small business community by making them aware of these private sector programs, and those of other agencies of the Federal, State, and local levels.

Mr. OLIN. Mr. Cox, I apologize for interrupting you, but I wonder whether it would not be of more value to the committee if you, instead of reciting all the activities that the SBA has, comment on the purpose of the hearing, which is to direct ourselves toward what policy changes could or should the Congress make to further competitiveness and more effective exporting.

Mr. Cox. Yes, sir.

Mr. OLIN. And perhaps if you could just off the top of your head, and from your experience, make some comments along those lines.

Your testimony will be in the record in its entirety.

[Mr. Cox's prepared statement may be found in the appendix.]

Mr. Cox. First off, I think that SBA can help in more outreach, getting the word down to the local level, to the small business community.

Mr. OLIN. Is there something we should be doing about that, outside of encouraging you and getting you to say that?

Mr. Cox. I think we are hearing what this committee's priority is, and we certainly will go forth with that.

In our 1988 budget, we have allocated something like $31 million to the SBDC Program. If international trade is a priority of this committee, then we would welcome your suggestions on the priority of that $31 million.

We are asking for that appropriation, and with it, if you write into the authorization that you want a certain amount of that in international trade area, then we——

Mr. OLIN. You are, basically, saying that you are looking for ideas from us on what you should be doing?

Mr. Cox. Well, I think——

Mr. OLIN. I was hoping to get something in the other direction.

Mr. Cox. Yes; I believe that if we are going to do more counseling, more training, out there, and utilize our resources, then we certainly have the resources, and we certainly have the local operations to carry them out. Within the SBDC law, as I understand it, there is a wide range of services that can be provided by them. If there is going to be a national emphasis on international trade, then I believe that should show up in the authorizing legislation.

Mr. OLIN. Yes; thank you very much, Mr. Cox.

Is there anybody else from the SBA who has something to say?

If not, I think I would like to turn to other members of the committee to see what questions they may have, and since our chairman occupied a fair amount of time, and I did, perhaps I will call on our minority leader here today, Mr. Gallo, for the first question.

Mr. GALLO. Thank you very much, Mr. Chairman.

And I want to thank the panel for your expert testimony. One thing comes out loud and clear. Each agency has its own outreach program, its own educational program, to try and entice and get small business involved in exporting.

One of the major problems that I have found, and by no means do I classify myself an expert in the area of trade, but through a seminar I held back in December, dealing with exporting and also State procurement and Federal procurement, it became clear that there was an awful lot of small businesses that would be interested in exporting, but did not know the first thing about where to go, or where to get the information. Furthermore, they were given a lot of the material that is produced by many of your agencies. You have here the service for exports from the U.S. Government. I mean, this book alone would scare the devil out of anybody that was contemplating getting into export. It took my staff about 4 hours just to find part of the information that they were looking for.

You have a whole host of books and pamphlets, gaining competitive edge for U.S. exports; we do it in New Jersey, too, with a New Jersey guide to export assistance; and it goes on and on.

I think one area that I would like you to address, and you have to some degree, but I have not heard the kind of answer that I would expect, is that somewhere this has to be coordinated. There has to be a point of entry for small business, for those that want to get involved. And if we took all the programs that are designed by the different areas in an effort to get small business motivated, we would have, I think, a coordinated effort.

That was mentioned by the chairman, of using the SBDC as a point to get this information, maybe with an 800 number, where that person or persons would have the ability to start that person down the road and follow through with that person. There are so many things that I think could be done if the entry point was one that had some real meaning to it—not, hello, we can send you this brochure, or we can send you that, but leading that person through. Many times you may tell him no, there is not a marketplace for that, or there is. That is a big help to a small business that maybe should not be involved in export, or even looking at it.

So my question to you is, can you give this committee suggestions as to how we could coordinate and have an entry point, one entry point, and what official way could we do that? Would SBDC be a proper place for that. I would like your suggestions.

Mr. Smart.

Mr. SMART. Mr. Gallo, we have in the U.S. Commercial Service, offices in 48 cities in the United States which are set up to do exactly what you describe, and we have been increasing our coordination with the Small Business Administration in an effort to tie our efforts together.

It seems to me that this is the coordinating spot that you are seeking, and that it already exists. We have had, obviously, as you describe, a problem with awareness. We have a program now in final stages of development with the ad council to put on an advertising campaign calling attention to these offices and to these services, and I would like to go back and put together something in greater detail than I can pull out of memory or than time will allow, and give you an outline of exactly how it works, and where we think there may be improvements that could be helped along by Congress. I believe the basic structure is already in place and spread around the country and organizationally properly linked with our outreach group overseas.

I also agree with you that it is not as well known as it should be.

Mr. GALLO. If I can continue, in these 48 States, do you handle the full range of export? I mean, would you be able to give information pertaining to Export-Import Bank and——

Mr. SMART. Yes, sir.

Mr. GALLO [continuing]. And all the way down the line.

Mr. SMART. We might not be the ultimate expert on whether a loan would or would not qualify and so on, but we clearly understand the fundamentals of how Eximbank works, and know the people to put the prospective borrower in touch with.

Mr. BOHN. Congressman, if I might add, we work very carefully and very closely with the offices to which Mr. Smart refers, and have had, by and large, very good success, not only in them coming in and understanding our programs and taking the time to come in and go through our certification programs, but also to a considerable extent of actually going up and turning over the stones and following up as you outline.

Part of the problem, in all candor, and the reason that you get those elaborate books and the great number of them, is really twofold. First, exporting is a complex business compared to simply selling in the next town or the next State. Second, we as a country, in my judgment, are still not producing enough people who understand both the exporting business and the need to export in terms of the national interest. So you have a tough time finding the people who can do what you say, whether it is in the Commerce Department or anywhere else. They work very hard at it, and we have had a very good relationship with them. They have been very helpful to us.

Mr. GALLO. We listened to testimony the other day, and they indicated that 250 companies do 80 percent of the export, and that there is the potential for small business numbering about 30,000 out there. So it seems to me that it would be very beneficial to not only those 30,000 small companies, but also very beneficial to our trade position to get them into the act, let them have a piece of the action. The only way we are going to get that is if in fact they know that there is a way of doing that. And again, everything focuses back to getting that person to be able to enter at a place where he or she is going to get the proper information at the right time.

Would you like to comment?

Mr. OLIN. Ms. Albertson, would you like to comment on that?

Ms. ALBERTSON. Thank you. I direct the SBDC Program for SBA, and the SBDC's already do a very large proportion of international trade activity. There are 49 SBDC's, that is, 49 lead institutions, but there are more than 500 organizations that deliver the services. As in New Jersey, Rutgers is the lead institution, but there are about 10 other organizations around the State that deliver the services. The whole concept of the SBDC as created by the Congress is to provide not only basic training and counseling for small businesses throughout, but broad-scale economic development outreach, research, all of the things that I have heard sort of bandied about here today as part of this committee's interest in international trade and how to get small businesses involved in it.

It seems to me there are two issues here, and I think that Frank Swain addressed them. There are two markets that need to be addressed, and it is whether one or both or all of these agencies might not address them.

One is the small businessperson who does not know about international trade, does not know about export, does not know how to go about it, does not know whether or not it is available, will not hear of it unless fully informed and instructed.

And then, of course, there is the large market that you describe of people who would like to get into it but have not the faintest idea, and there is a sort of impenetrable barrier of agencies and Federal people and booklets and pamphlets and all that sort of thing.

So it seems to me that the Small Business Development Center Program is already being very useful and can continue to be useful, depending on the priorities established, as Mr. Cox said, by this committee.

Mr. OLIN. Would the gentleman yield to the Chair?

Mr. GALLO. Yes.

Mr. OLIN. This may be a question you do not want to answer, but you are implying that the SBDC Program is very effective in meeting the need, which is to know about the market, and then to know how to get into it. Now, beyond that there is the management skill and the financing, but this really comes first.

And yet the administration is still trying to shut down the SBDC Program. Does that imply that—I do not know whether you can answer this or not, you probably cannot—that we have not abandoned the idea of shutting down the agency?

Ms. ALBERTSON. I would like to defer that question to Mr. Cox.

Mr. OLIN. Mr. Cox, that is a very wise answer. But literally, it is incredible that, on the one hand, someone says, we do not hear from anybody, and then the SBDC says we have identified 50,000 people that are interested in exporting. And then on the other hand, there is another arm that wants to shut down that activity. What is going on?

Mr. COX. OK. The Congress, of course, has a proposal from the administration to phase out the Federal funding of SBDC, which is, from the standpoint of the administration, a little different than closing the program down. That, of course, is still on the table.

I think that we can still talk about SBDC's and what they can do, since we have got, even next year, $31 million to work with.

Mr. OLIN. As a last gasp, you mean?

Mr. COX. No.

Mr. OLIN. I am not sure I really understand what you are saying.

Mr. COX. The administration feels that the SBDC's—it is not the death bell of the SBDC's if Federal funding were phased out. And so we would still have——

Mr. DEFAZIO. Would the chairman yield for a moment on that?

Mr. OLIN. Certainly, Mr. DeFazio. I apologize for not looking down that way.

Mr. DEFAZIO. No; that is fine. I would like to pursue this kind of bizarre logic that we have heard that the SBDC's are now somewhat focused on this issue, or a focal point could be more focused; as you said, give us the message, give us the mandate.

And on the other hand, now we are saying that phasing them out is not going to be detrimental to the SBDC's or this effort or in fact, perhaps, to an enhanced effort in the area of export development.

I guess two questions. First, the problem of our trade balance is a national problem. I mean, it is not something we should delegate to the individual States; is that correct? I mean, we should say that it is a national priority, it is a national problem.

And second, generally, we deal with national problems on a national basis, and you are saying that to take out this funding, this $31 million, to phase it out will not affect the program. Well, in my State we have been hit by the recession for 6 years now. We are a potential and are in fact a net exporting State, the State of Oregon on the Pacific rim. Great potential on the Pacific rim.

We are putting up 80 percent of the money for our SBDC's now, and you are telling us, oh, well, you are just going to have to put up the other 20 percent? Where are we going to get it?

Mr. Cox. No; we do not foresee that. There are other avenues of funding. SBDC's at the current time are contracting with public and private entities on other projects, things of this nature. There is private sector—a lot of large corporations are starting to assist SBDC's. So, there are other avenues than the Federal program.

Mr. DeFazio. But if they could help us with the balance of trade, if they could encourage these exports, would not the return be greater than this minimal investment on the part of the Federal Government, the $31 million, when we are talking about $160 billion, $170 billion—who knows what it will be—trade deficit?

Mr. Cox. I have not seen any figures where we are going to have a big, whopping change in the trade deficit because of some small businesses getting into international trade. Now, maybe over the long run it certainly is going to help.

Mr. DeFazio. Yes; well, I will wait for my series of questions to get to that. I have questions on that.

Mr. Olin. I would like to call on Mr. Smart, who was interested in responding to your question. Let me call on him first, and Mr. Campbell will be next.

Mr. Smart. Yes; Mr. DeFazio, what we are talking about here on improving export capability for small businesses, or for that matter, for any businesses in the United States, is terribly important to our long-term industrial preeminence and to our standard of living. But I would submit that it has relatively little to do with our trade deficit.

The trade deficit is, basically, a phenomenon of macroeconomic factors relating to the fact that U.S. private savings are inadequate to cover both investment and the net fiscal deficit of government at all levels, and that forces money to flow in a way that creates a trade deficit, or rather, a current account deficit. And that what we are talking about here would have, perhaps, some but not very large impact on that, despite how important it is to our long-term competitiveness.

So, while the two call attention to each other, I am not sure that one is that closely linked with solving the other. And I throw that out because I thought it had sort of come up in this discussion.

Mr. Olin. I would like to call on Mr. Campbell now for questions.

Mr. Campbell. Thank you, Mr. Chairman.

I would like to, maybe, just change gears a little bit, but since Mr. Smart was the last to speak, I would like to ask you something. I asked a question of a panel yesterday, probably prematurely; I probably should have asked it of you, because they did not have a very definitive answer.

And it was not related to exports as much as imports. It is my understanding that we have about a $60 billion counterfeiting system of American products that are being made in foreign—well, they are copies of American things being made in foreign countries. They are imported over here, and they go through duties here, after which the paper labels are taken off and permanent labels of American brand names are put in, clothing, shoes, any number of things, handbags, and so on.

I was wondering, do you have the authority, department authority, within the Department of Commerce, to require points of origin to be indelibly stamped or sealed or put or affixed on foreign products when they come in, so that could be prevented?

Apparently, it is not really a problem with the people that are making it as it is with somebody here after it is imported.

Mr. SMART. The problem exists at a variety of levels, and the fraudulent activity you describe takes place in various locations. You start out with the fact that there are a number of countries in the world, many countries, that do not have adequate intellectual property protection laws, or if they have good laws, do not enforce them properly, because, frankly, they do not create much new in the way of trademarks or patents or what have you.

And so, ripping us off is a convenient way for them to get rich. We have a program going now which I think is dealing with 19 separate countries, trying to get them to improve their protection and/or their enforcement, and we also have succeeded in getting intellectual property protection in as a subject of the GATT round. So that we are addressing that at the foreign level for exactly the reasons you describe.

There is a second problem called gray market in which people who are licensed to use a trademark, let us say, in the United Kingdom will, because of currency exchange or cost differences, sell that product in the United Kingdom with a legitimately applied U.S. trademark for distribution in Britain to a middleman who will then bring it back to the United States and hitchhike on the promotion and whatever else that the United States owner of the trademark has spent in the United States. That type of gray market activity is not specifically precluded. There is quite a debate within the administration as to whether it should be or not.

As far as mislabeling stuff, bringing it though customs properly, then changing the labels, that seems to me that is an act of fraud, but I do not know specifically what laws we have other than that to address it.

Mr. CAMPBELL. Well, I think so, too.

If I can continue, a gray market, as I understand, one of the biggest areas is automobiles. But that is totally different than what I am thinking of. We have things written under the fraud laws, but we cannot seem to police it over here. It seems to me that if we cannot police it and we cannot catch the people and prosecute them, maybe the second best thing is to make sure that when it comes into the country it cannot be changed; it is stamped. If it is a metal product, it is stamped on there so that the thing cannot easily be changed.

As I understand your testimony, you are saying that we are trying to work with other countries to convince them that they should tighten up the restrictions and therefore prevent it at the point of origin; is that what you are saying?

Mr. SMART. Yes; stop putting the alligator on the polo shirt without the approval of the alligator trademark owner. The question you raise I will get you an answer for, because I do not know the answer to it right here.

Mr. CAMPBELL. Yes; I do not think that what I am asking, really deals with those people.

Mr. SMART. No.

Mr. CAMPBELL. If we can convince them to have some ethical behavior when they are exporting to this country, so it is not changed, that is one thing. Apparently there is some kind of a clandestine system, though, to change a lot of it when it gets here. I do not believe it has anything to do with smuggling. It has to do with changing it after it gets here and then using American brand names after it gets here.

I have been approached by several people who felt that they have had products—I do not know what the word is for that, plagiarized. It is not exactly counterfeited, but certainly it is illegal in this country, and it is being done. No one seems to know how to stop that, since we already have the laws on the books and cannot police it.

Mr. SMART. I had not heard of the problem, and I will get you an answer.

Mr. CAMPBELL. I appreciate it. Thank you.

Mr. OLIN. Mr. DeFazio, do you want to ask more questions? I want to make note of the fact that some of our witnesses may be leaving here. I do not know just when, but we have word that they will be leaving fairly soon. You might save a little time for Mr. Price.

Mr. DEFAZIO. Sure, I will if I move quickly. To Mr. Cox, on page 5 of his prepared testimony he said, "During fiscal 1987 increasing our efforts on outreach to small business communities, identify those small businesses with export potential and interest." And my question is, how? What specific steps are you going to take to identify them? Through what part of the agency?

Mr. COX. We have taken steps already sir, on drawing from the names from our PASS system, the procurement source system. We will be contacting those companies and making them aware of programs available to them.

Mr. DEFAZIO. I am particularly interested in the SBDC's. We have an International Trade Program at Oregon, although it was not mentioned in one person's testimony here. What about this enhanced role for SBDC's in this area?

Mr. COX. The SBDC's currently put on international trade seminars, conferences, around the country, along with SCORE and chambers of commerces. We can get you a list of all those events if you would like.

Mr. DEFAZIO. OK. But also a more active or continuing counseling role beyond the introduction in a conference. Is that correct?

Mr. COX. Yes.

Mr. DEFAZIO. Retired executives, people who are familiar with the export business.

Mr. COX. Yes.

Mr. DEFAZIO. And you think that is a good program and it has helped enhance some business' capability to export?

Mr. COX. Very much so.

Mr. DEFAZIO. OK, that is good. One very quickly to Mr. Swain. This is an issue that came up yesterday having to do with impediments, regulations that are impeding the entry into the export market by American firms. We all know about the dispute between the State Department and the Defense Department and Commerce in that area.

But I am just curious. You talked quite a bit about domestic barriers, internal barriers. Is there an effort going on to identify barriers other than the ones you are mentioning here, which are sort of the ideological ones; Davis-Bacon, and cost of business here, and talk about that in terms of competitiveness.

But the actual nonproductive things, the interagency disputes and squabbles beyond the well-publicized one here. Other things that we were led to believe. There are quite a few impediments in regulations that do not seem to be necessary. Is there an effort to identify those?

Mr. **Swain**. The White House Conference on Small Business, last year, did in fact identify 60 some impediments. And those that I mentioned were ones that, whether you regard them as ideological or not, are certainly close to the heart of small businesses. But Mr. Smart in his testimony alluded to the fact that there are significant ongoing changes within the Commerce Department on Export Act administration regulations and paperwork, which we have certainly been happy to consult with them on.

And to the extent that the Federal Government regulates exports, I think that Mr. Smart is better qualified to say, there is some significant and beneficial changes. Most of the export problems, the questions on whether to get involved in exporting or not really are not governmental problems. They are business problems.

But to the extent that the Government does create problems, I think that Mr. Smart could, if you were interested, describe further what his department was doing.

Mr. **DeFazio**. So the mention of the vice president reconvening an executive branch review group, they will deal not only with things that are seen as domestic policy issues which have been debated by this Congress since the administration has been in office and rejected, but actually inefficiencies in the Government and interagency inefficiencies.

Mr. **Swain**. Absolutely sir. The vice president's task force is in fact a regulatory review task force.

Mr. **DeFazio**. OK. Thank you very much.

Mr. **Olin**. Mr. Price?

Mr. **Price**. Thank you, Mr. Chairman.

I would first like to address a question to Mr. Shane. This committee received testimony yesterday about the SBIR share of Federal R&D and it was suggested that the time was right to increase that percentage above the current 1.25-percent level. What is your view of that recommendation?

Mr. **Shane**. This recommendation came out of the White House Small Business Conference. If I recall correctly, it was to rise to 3 percent. We would not concur with an increase of this magnitude at this time. We would concur with part of the increase.

Taken literally, a 3-percent increase would be an increase of 140 percent to each agency. The agency's SBIR Program budgets are set by their R&D budgets, and multiplied by a fixed percent which gives us an uneven amount of money between the various agencies.

The larger agencies, being the Department of Defense, the Department of Energy, NASA, and HHS, would probably struggle greatly under an increase of 140 percent. The smaller agencies, with the smaller dollar amounts, would benefit from this because it is difficult to have a good R&D Program when you are only making 30 or 35 awards each year. So we would consider an increase in that particular area to be of value.

I think if we went with the suggested increase we would suffer a blow to the program which I am against, as we would be going to quantity instead of quality. I think it is highly important to keep that distinction in mind. To tell the Department of Defense to increase their awards from approximately 2,000 to almost 4,500 a year would lead us down the path of quantity, not quality.

Mr. PRICE. You say in your testimony we are dealing with 11 participating agency budgets. And for the first time this year all of them have reached that legislative percentage.

Mr. SHANE. That is correct.

Mr. PRICE. Are there great differences among those agencies?

Mr. SHANE. Vast differences, awards by the Department of Defense of approximately 1,000 to 2,000 to smaller agencies with 30 or 35 a year.

Mr. PRICE. Does that lead you to question the utility of an across-the-board percentage requirement of this sort?

Mr. SHANE. I think it raises problems. And I think it raises technical and administration problems in conducting a proper R&D effort. When you are conducting an R&D effort I think you have to have goals that you are heading for, whether they be at the Nuclear Regulatory Commission or EPA or the Department of Defense. You have to have a technical goal that you are trying to achieve or solve.

Furthermore, it hampers the internal interest in the agency because of the size of the amount of the award and the goals.

Mr. PRICE. Thank you. I am aware our time is limited. Let me just turn quickly to one remaining matter.

I am very much interested in the possibility of enlisting our university community more fully in this effort. I suppose it is Mr. Cox's testimony that most directly speaks to that. But I would welcome comments from anyone on the panel.

Mr. Cox, you talk about the university-based Small Business Institute's Program and the role it has taken in providing international trade counseling and research. I wonder if you could elaborate on the university role. What are the factors that you identify with that role when it has been successful? How might that role be enhanced?

Mr. COX. The Small Business Institute Program is in approximately 400 universities nationwide. It deals one-on-one with businesses on business problems and research in that area. We would look to SBI to take on a greater role in this.

This is done under a contract per case cost. The Government pays the university for providing the service. The type of cases are really dependent on the priorities at the local level. We could raise the priority of international trade to utilize that program to a greater degree.

Mr. **Price**. Are there any other members of the panel that might have some comment about the extent to which the university community has been involved in these programs? Or how we might enhance that?

Mr. **Swain**. I would simply say, Mr. Chairman, that what Mr. Cox was saying earlier is that universities are involved in a variety of programs to assist small businesses. Some significant number of them direct their programs toward assisting small businesses to export. Others to acquire high technology. Others to do other things. And certainly that is a system that seems to work reasonably well.

If the committee is interested in directing the SBA to pay more attention to exporting and less to high-technology development or less to procurement or something, that is certainly a direction that we would take seriously. But I think the implication of Mr. Cox's comments are important. We are constrained to some degree. We have to pick and choose which are the priorities.

Mr. **Price**. But surely to the extent we do direct ourselves toward promoting international trade, the universities would have a major contribution in helping small businesses. And I would think we should give a great deal of thought to how university participation might be enhanced.

Thank you, Mr. Chairman.

Mr. **Olin**. Thank you. We have another gentleman who has joined us. Mr. Rhodes, do you care to question the remaining witnesses? We lost two of our witnesses.

Mr. **Rhodes**. No; thank you, Mr. Chairman.

Mr. **Olin**. I might observe we only have people left from the SBA. I am not sure that the SBA really has grasped the desire at this kind of hearing.

I recognize the fact that the SBA cannot be all things to all people. They have certain financial restraints—always will have. And yet, what we are looking for is your ideas from your experience. You have had broad experience with small business obviously, far more than some of us. We want your ideas about what modification in national policy would be beneficial.

It seems that the most that we get is a recitation of what the SBA is already doing, which is interesting. But I do not know whether that implies that the present program is optimum for the SBA or not. I suspect but I do not know if this comes about because you are in a transition period right now, which we all recognize, or what it comes from. But it bothers me. That really does not require comment.

I would hope you could be more aggressive in bringing forth to the committee ideas about the problem of competitiveness and increased foreign trade that we are interested in. Do you have any comment, Mr. Swain?

Mr. **Swain**. I did attempt to set forth in my testimony, and certainly because of the timeframe we did not get fully into it, a variety of issues that we do specifically see. But the issues that I alluded to in my testimony were, admittedly, not how we should run the SBDC Program differently.

I think we have plenty of ideas on that and I am certainly sure that Mr. Cox and Mrs. Albertson would be glad to give you a variety of ideas of the things that they perceive that work well within the SBDC Program as opposed to those that do not work very well. We have 48 or 49 of them out there and certainly not all of them are doing a great job. Some of them are doing much better than others and they can certainly advise you on that.

In terms of national policy, we think the three issues are; first, avoid protectionism. Small businesses are free traders. They do not like protectionist legislation. Second, get small businesses more involved in the current process whereby we are negotiating agreements with our foreign partners. We have now done that informally with the special trade representatives office. And certainly, to the extent that foreign trade issues are settled many times continents away, and small business finds out about it when it is too late, an earlier warning system, consultation among the relevant Federal agencies. This is extraordinarily important.

I do not know whether that can be legislated. Probably it cannot be and probably it ought to occur on its own. But I think that is a priority to the small business community. Identify better coordination as a priority.

And third, the priority of solving some of the issues that cost small businesses a lot of money right now, for example product liability, the employee benefits issues, some of the regulatory issues that we have domestically. I think that they do have a very direct impact on international trade. And any time the committee is interested in any more detail, we would be happy to try to provide it.

Mr. OLIN. I thank you for those comments. Do any other members wish to speak? Mr. Gallo, any other questions?

Mr. GALLO. No; thank you.

Mr. OLIN. If not—yes sir.

Mr. SHANE. Mr. Chairman, if I might make the last comment.

Mr. OLIN. Yes; go ahead.

Mr. SHANE. I really do not believe that high technology is the problem that we are really dealing with here today and I humbly raise the point that the Japanese did not invent the car, the television set, VCR's, cameras, or binoculars. They went into and excelled at production and marketing. They took our ideas and moved them in a production and marketing track through a well-organized set of steps with their Government assisting to ease the barriers. I do not think high technology is the country's problem.

I think the solution to the export problem is getting our products made with quality and timeliness, and aggressively marketing overseas while breaking down internal barriers. I would raise the point that in the SBIR Program in the first 3 years of the program, 65 percent of our winners never did business with the Federal Government before because of perceived barriers. Without the removal of these barriers they still would not be working with the United States Government in trying to solve high-technology problems.

So I would suggest that that this should be taken into consideration.

Mr. OLIN. A very valid observation. I would like to thank you all for testifying. We are pleased to have you here. Thank you. The meeting is adjourned.

[Whereupon, at 2:40 p.m., the Committee adjourned, subject to the call of the Chair.]

APPENDIX

Prepared Statement of John A. Bohn, Jr., President and Chairman, Eport-Import Bank

Mr. Chairman, Members of the Committee:

It is a pleasure to appear before the House Small Business Committee and I thank you, Mr. Chairman for providing me with the opportunity to review with you the efforts which the Export-Import Bank has made in recent years to tailor its programs and products to the needs of small business. At the outset, let me say that we believe the future competitiveness of the United States and our ability to tackle the gargantuan trade deficit hinge in large part on the competitiveness of our small and mid-size companies; that is where we can continue to expect the greatest growth in job creation and gross national product.

Despite comments in the past that Eximbank has been largely the financing arm of some of America's largest exporting companies, let me assure you that we are deeply committed to working with and promoting the small businesses of America in their export drive. We believe that America's small businesses must be able to market their products worldwide, and we believe that Eximbank can help them achieve their goals.

In 1983, Congress enacted provisions to ensure that Eximbank programs would be made widely available to small business. In the next few minutes I would like to review what we have been doing since then to implement these provisions. I also want to emphasize that we plan to do more. Since last year -- and even before enactment of the amendments to our charter in October 1986 -- we have been engaged in the most thorough review of the Bank's programs since 1960. The results of this review will be embodied in new programs which go into effect on May 1. Some of the program features will be directed at small businesses; others will affect all exporters, including small businesses.

In the near future, I will be announcing specific program improvements targeted at small businesses. At the present time, let me just say that we have been guided by the realization that Eximbank must assume a broader range of explicitly defined country and transaction risks than it has previously. Programs and procedures need to be simplified, streamlined and internally consistent. They must also be accessible to the widest variety of potential sources of export finance, including capital market participants.

Now let me tell you about the measures we have taken since 1983 to help small businesses. One of the requirements of the 1983 legislation was to establish a "small business set aside" in which we were instructed to allocate increasing levels of our annual authorizations to small businesses. This ranged from 6% in the first year to 10% in FY 1986 and thereafter.

I am pleased to report that Exim has more than met the expectations of the "set aside." In 1986 small business accounted for 23.7% of our authorizations. In dollar terms, small business accounted for $1.44 billion of the $6.08 billion authorized.

Perhaps as important as the numbers is the commitment that the Eximbank Board and staff have made to small and mid-size businesses. This is seen in the development of new programs and distribution systems, calling efforts around the country. and the ongoing improvements to our programs.

Our goal is to provide these companies with the full range of support which they need in order to compete in today's marketplace. We recognize that, in addition to the broad difficulties facing all exporters over the past several years brought on by the LDC debt crisis, lower demand for U.S. goods, and until recently an overvalued dollar, there are several chronic difficulties relating more to the small and mid-size business exporters. These include the difficulty of finding a lender willing to work on small transactions, getting assistance with the paperwork associated with all forms of international trade, and getting financial support at a reasonable cost.

We found, for example, that one of the most difficult problems small businesses face is obtaining working capital support in order to purchase raw materials, meet payrolls, and produce the goods and services for sale. If they cannot overcome this obstacle, all other issues are moot. We found good, well-managed companies unable to take advantage of export opportunities for the lack of working capital.

We created our Working Capital Guarantee Program in 1984 to remedy this situation. Under this program Eximbank guarantees working capital, pre-export loans to U.S. businesses. Many of these are to emerging companies, others to small businesses which have significant opportunities to increase their level of export business. Since 1983 we have approved 104 cases, with a value of $110 million. Businesses in 26 states and the District of Columbia have benefitted from the program. There has been considerable diversity in the products sold, ranging from wood products, to machinery, and high tech products. Exports under this program have gone forward to 27 countries. There is a great deal of momentum in this program. In the first six months of this fiscal year our authorizations will reach or exceed the level for all of 1986. Additionally, we took a hard look at the program and are now considering exporter and lender suggestions concerning documentation, collateral, fees and the delegation of authority.

After small businesses have made arrangements to assure adequate working capital, they need protection from foreign repayment risks. As commercial banks become more risk averse and sources of political risk insurance become fewer, many choose to insure their sales with the Foreign Credit Insurance Association, our insurance affiliate. In fact, the majority of all FCIA policy holders meet the SBA definitions of small business. Small businesses have found that our programs made it possible to continue to sell in tough markets abroad through our facilities for Mexico, Brazil, Nigeria, Jamaica, Central America, the Philippines, and others.

While most businesses use FCIA's short-term deductible policy, we offer an insurance program for companies which are new to export. Special enhancements, such as lower premiums and an assurance to lenders that they won't be penalized for mistakes made by inexperienced exporters, make this policy especially useful to companies just beginning to export. We are in the process of simplifying this policy and quantifying the risks in such a way that lenders will be able to treat international trade in an operationally streamlined fashion.

We developed an Umbrella Policy so that intermediaries such as state agencies, insurance brokers, and banks would market and administer policies on behalf of small businesses. At this time we have 23 umbrella policyholders, representing an aggregate of 132 exporters under these policies.

Eximbank has paid particular attention to the small business community's needs for medium term financing of capital goods sales. Under our Small Business Credit Program, we commit to making fixed rate loans without requiring evidence of foreign, officially supported competition. Earlier this month I announced two major improvements in the medium term programs. First, businesses will now have direct access to Eximbank for the medium term programs. This will enable them to get preliminary commitments from Eximbank which they can take to their choice of lender. Also, in order to motivate lenders to support the smaller transactions, we have enhanced our intermediary loan program. For smaller transactions we will provide loans at 1.5% below the applicable OECD consensus rates, as opposed to a discount of .5 - 1.0% for larger transactions.

No matter how good the programs are, they still require a distribution system to get them into the marketplace. Eximbank organized a Marketing and Program Development Division in 1984, headed by a Vice President. It coordinates bankwide efforts to reach small businesses and to work with the program divisions to create and implement new programs. In FY 1986 marketing division personnel made presentations to 5000 people in 36 states. These efforts were coordinated with FCIA regional marketing offices in New York, Miami, Houston, Los Angeles, and Chicago.

Developing intermediaries is of utmost concern to me. With a small staff we need qualified and motivated intermediaries to reach all of the prospective small and mid-size businesses which could benefit from our programs. Commercial banks have been our most significant distributors. So, to be sure that they were well-trained in Eximbank programs, we began an intensive four-day program that led to bank certification. To date nearly three hundred banks, large and small, have been certified.

These seminars have also been well-attended by representatives of state agencies, and field offices of the Department of Commerce and the Small Business Administration. In fact, we developed a joint guaranty program enabling the SBA to double its working capital guaranty capacity to $1,000,000. This has been used on seven occasions.

Additionally, we have introduced a specially designed program for trade associations. I am pleased to report that the first such policy is already in operation for the National Machine Tool Builders Association. This policy packages short and medium term insurance. The association is administering the policy on behalf of its members, providing such useful services as making premium payments and shipment reports, and filing claims. Eximbank staff and association executives are jointly marketing the policy. In fact this month they met with member companies in Washington, Chicago, Hartford and Detroit. An important element in this package is that a commercial bank was selected to provide financing for all insured transactions, even for small amounts that had been difficult to finance in the past.

Mr. Chairman, since our 1983 meetings, Eximbank has been aggressive and innovative in its support of small businesses. We have developed new programs. We haven't been afraid to take risks. Some concepts and programs have worked better than others. We are now at a stage where we have evaluated the programs, put our emphasis where it is likely to be most effective, modified programs in conjunction with user suggestions, and are ready to do still more. You have given us the tools, and we have the attitude and enthusiasm to do a job that we all recognize is important for American exports and for jobs at home.

EXCERPTS FROM THE 1985 ANNUAL REPORT TO CONGRESS BY THE EXPORT-IMPORT BANK OF THE UNITED STATES

Helping Small Businesses Export

During fiscal 1985, Eximbank continued and intensified its efforts to reach out to small businesses and help them use the entire range of export support programs Eximbank offers. Eximbank authorized $1.9 billion in support for exports by small businesses. This total represented a 5.1 percent increase over fiscal 1984 authorizations for small businesses, and 13.7 percent of the total budgetary authority available to Eximbank in 1985.

Use of the Working Capital Guarantee program, which assists small exporters to obtain pre-export financing, was especially strong. Since the program was introduced in 1983, Eximbank has authorized 49 Working Capital Guarantees totaling $55 million. Fiscal 1985 authorizations accounted for 65 percent of the total number of Working Capital Guarantees and 49 percent of the dollar total approved since the program's inception.

Eximbank's small business authorizations in fiscal 1985 included 87 loans totaling $80 million and 804 guarantee and insurance transactions totaling $1.8 billion. Of the small businesses receiving Eximbank's assistance during the year, 142 had not previously participated in Eximbank's programs. Of the small business commitments entered into during the year, 320 totaling $68 million were in amounts less than $500,000. All of Eximbank's small business authorizations assisted exports by individual companies, none by consortia of exporters.

Eximbank's small business authorizations, by program, follow.

	Small Business Authorizations			
	1985		1984	
Program	Amount $ Million	No. of Transactions	Amount $ Million	No. of Transactions
FCIA Insurance	$1,649	728	$1,494	861
Working Capital Guarantees	27	32	18	10
Bank Guarantees	37	26	36	30
Financial Guarantees	103	18	112	21
Total Guarantees & Ins.	$1,816	804	$1,660	922
Small Business Credits	$23	64	$41	77
Medium-Term Credits	19	12	5	4
Direct Credits	38	11	98	17
Total Loans	$80	87	$144	98
Grand Total	**$1,896**	**891**	**$1,804**	**1,020**

The following pages illustrate some of the many ways that small companies worked with Eximbank on actual export transactions in fiscal 1985. Eximbank's efforts to assist more small companies to understand and use its services are summarized in the Review of Operations section.

Jernigan Trading Company

Jernigan Trading Company is a family-owned timber trading company based in Knoxville, Tennessee, with a total of six employees. Its principal customers are Western European mills producing veneer for manufacturers in the paneling and furniture industries. To fill its export orders, Jernigan purchases white oak and black walnut logs and standing timber growing in forests from Alabama to Arkansas.

When company president Victor Jernigan traveled to Europe last year, he faced a difficult selling job. He explains: "Dollar fluctuations in Europe have been a nightmare. While the European furniture and paneling industries may be stable, they can't raise the price of their final product enough to keep up with the dollar." To overcome this hurdle, Mr. Jernigan offered his buyers extended credit terms. By doing so, he was successful in obtaining $1.7 million in new orders.

Since he had to pay cash for the timber to fill the orders but had to wait for payment from his customers, he needed to borrow working capital. When he approached prospective lenders, however, he found that he could not arrange the amount of financing he needed with his collateral of export receivables and an inventory of logs.

Mr. Jernigan found the solution to his cash flow problem at an Eximbank Small Business Seminar in Nashville. At the suggestion of a commercial banker he met at the seminar, he applied to Maryland National Bank for a line of credit.

Maryland National Bank agreed to extend a $479,000 revolving credit line secured by inventory and accounts receivable, if Eximbank would extend its guarantee on 90 percent of the outstanding amount of the line. Eximbank approved the Working Capital Guarantee requested by Maryland National.

Mr. Jernigan says, "I provide a buying service for primary quality manufacturers who absolutely must receive their raw materials on time. Without the help I received from Maryland National and Eximbank, it would have been really difficult to meet my European customers' needs."

RD Systems

RD Systems began operations in 1973 when engineer James Ribordy began designing special purpose assembly machines in his basement. While the Roscoe, Illinois, company is still small, it has grown dramatically and now has more than 25 employees.

The company has designed more than 600 production machines, including electronics system equipment, pharmaceutical machines, special purpose robots and more than 100 automated battery assembly machines. Today, an estimated 60 percent of the alkaline batteries manufactured in the United States are made on machines designed by RD Systems, and the company's sales are expanding through exports.

RD designs, engineers and inspects equipment, while machine shops manufacture the components. RD's first export order came almost by accident. When another company bidding on an export contract with RD as subcontractor dropped out of the competition, Tadiran, the Israeli purchaser, asked RD for a quote.

After RD won the $1.6 million export contract to design and produce six battery assembly machines, Mr. Ribordy and his daughter Jo contacted the new U.S. Department of Commerce office that had just been set up in Rockford, Illinois. They attended a series of Commerce "how to export" briefings and a program on working capital and export financing conducted by an Eximbank marketing officer.

Bank Hapoalim of New York was able to extend a medium-term export loan to Tadiran by obtaining a fixed-rate funding commitment under Eximbank's Small Business Credit Program. RD arranged the working capital it needed to fill the order with a $700,000 revolving line of credit from Macktown State Bank of Rockton, Illinois, and its larger correspondent, Marine Bank, N.A., of Milwaukee, guaranteed by Eximbank's Working Capital Guarantee.

The first-time exporter, its small town bank, a larger correspondent bank, the buyer's bank, and two U.S. Government agencies all came together at the right time and place to make this export possible. RD's first export sale exceeded all other sales for the year and has led to subsequent orders from Tadiran.

Roscor Corporation

The Roscor Corporation of Mt. Prospect, Illinois, has a tight-knit family management. Company president Phillip Roston brought his two sons into the company on a part-time basis while they were still in high school. Both are now full-time executive vice presidents. Mitchell oversees sales and financial aspects of the company. Paul is responsible for the company's technical services. Together, they have helped the company expand from six employees in 1971 to a record 110 last year.

Roscor was started in 1917 as a camera store. Today, the company operates two retail camera stores, but it also distributes, sells, leases and repairs a full line of advanced video equipment and systems, performs specialty editing and copying, and designs, constructs and assembles television studios.

When the Korean Broadcasting System selected Ikegami Electronics of Japan to supply two mobile television production trailers for use at the 1986 Asian Games and the 1988 Olympic Games, Ikegami subcontracted most of the order to Roscor. Each of the 44-foot trailers was to be designed and equipped to receive signals from up to 10 cameras and to permit all editing, special effects and switching to be carried out within the trailer.

In addition to its engineering and manufacturing services, Roscor's portion of the contract included the trailers as well as a majority of the electronic equipment and other materials. To fill the order, Roscor had to purchase more than $3 million worth of equipment from other American suppliers. Since it would not receive payment until shipment, it needed to borrow a substantial amount of working capital.

With Eximbank's Working Capital Guarantee, American National Bank and Trust Company of Chicago was able to provide a $3.17 million revolving working capital line of credit, enabling Roscor to finance its inventory purchases and production costs.

Roscor successfully completed its first major export contract and paid off the loan. It is now exploring new opportunities to penetrate Asian markets.

Biomedical Exchange International

Physician William Helvey and electronics engineer Earl Jackson have become specialists both in the application of advanced technology to health care and, more recently, in the intricacies of export financing. They helped to develop the biotechnology for the U.S. manned space program in the 1960s and have kept abreast of advances ever since. Their export activities began in the early 1970s and, since February 1978, they have owned and operated their own very successful export trading company, Biomedical Exchange International.

The four-employee trading company specializes in providing export services to emerging American high technology medical equipment manufacturers.

Partners Jackson and Helvey attend the major medical conventions to keep abreast of technological developments and to meet with clients and potential clients. They report that American cardiovascular equipment is the best in the world, because of the great advances brought about through American research. Among the many leading-edge products exported by Biomedical Exchange are Gish Biomedical's systems for regulating blood temperature during open heart surgery, Zymed's Holter monitoring system in which a scanner reads a cassette recording of a patient's electrocardiogram taken over a 24-hour period, and specialized catheters manufactured by Devices for Vascular Intervention, Nova Medical and Advanced Cardiovascular Systems.

All sales are exports and are generally on letter of credit or, for established customers, on 30-day open account. To accommodate increasingly large orders from its credit customers while moderating risks, the company turned to FCIA Export Credit Insurance. Biomedical obtained a New-to-Export insurance policy in March 1984. A year later, after insuring more than $1 million in export credit shipments, it graduated to a Short-Term Deductible policy.

The company's sales have grown dramatically, from less than $185,000 in 1981 to more than $5.7 million in 1985, an average compounded growth of nearly 150 percent per year. Much of the increase represents repeat orders from satisfied buyers in Japan, Australia, and New Zealand. FCIA insurance has helped the company's sales to grow much faster than they could have otherwise.

RAMCO and Waste Heat Technologies

Coal-fired power plants throughout the People's Republic of China will become more fuel-efficient with the installation of heat pipes manufactured in a new plant in Henan Province. The heat pipes will be produced with equipment and technology exported by two small American firms aided by Eximbank's Working Capital Guarantees.

RAMCO, Inc., is a 14-employee firm in San Diego, California, founded in 1976 by Richard A. McCormack. Waste Heat Technologies, Inc., of Wadsworth, Ohio, has 39 employees and was founded by T. S. Formaz and Rik Underman in 1983. The two companies won separate contracts totaling $2.24 million from China North Industries Corporation (NORINCO) for the heat pipe manufacturing project at the Zhongzhov Machineries Factory.

Waste Heat Technologies supplied specialized machine tools, brazing furnace, soldering station, computer, computer software and technology for the production of the external finned tubing, a major component of the heat pipe. RAMCO provided specialized machine tools, computer software and technology to perform the intricate machining on the inside of the tube as well as cleaning, evacuating, filling it with working fluid and sealing.

Waste Heat's bank, Centran Bank of Akron, referred its client's request for export-related working capital to the International Department of its larger affiliate, Central National Bank of Cleveland. Central National's $305,000 line of credit, guaranteed by Eximbank, enabled Waste Heat to fill its $1.37 million contract.

RAMCO's bank, the Bank of La Costa, California, had reached its lending limit for the company but, with Eximbank's guarantee, was able to provide the additional $230,500 RAMCO needed to fill its $870,000 contract.

Following successful completion of these first Chinese contracts, RAMCO and Waste Heat Technologies each began negotiations on subsequent joint ventures with NORINCO. In addition, both companies are expanding into other Asian markets.

RET Corporation

The world's original use of agricultural irrigation is thought to have occurred along the banks of the Nile River in Egypt when the first seeds were sown in mud left by subsiding flood waters. Today, RET Corporation, a 16-employee design and engineering firm in Springfield, Virginia, is applying the most advanced hydrological data collection technology to develop the Nile River Irrigation Data Collection System.

Numerous stations will be located along the Nile and the extensive network of canals in Egypt to monitor water level, rainfall, water temperature, evaporation and wind. Collected data will then be transmitted to two computer-equipped master control stations by meteor burst communications equipment, bouncing signals off the ionized trails left by meteors entering the earth's upper atmosphere. The control stations, at Cairo and at the High Aswan Dam, will analyze the data and allow for directing the flow of irrigation water where it is needed.

RET's $3.3 million turnkey contract with the Ministry of Irrigation of the Arab Republic of Egypt covers system and equipment design, hardware procurement, installation and software development and project management, including training of Egyptian personnel.

The project was funded by a grant from the U.S. Agency for International Development, but the contractor needed working capital to cover the large start-up costs. American Security Bank in Washington, D.C., already had a substantial exposure with the company, but it agreed to extend additional financing of $500,000, if it could obtain Eximbank's Working Capital Guarantee.

Since RET was founded by Raul E. Truffat in 1978, the company has specialized in the application of high technology to projects in developing countries. Most of its business has been in Latin America. The Egyptian project offered an opportunity to expand into the Middle East.

JERNIGAN TRADING CO.
Timber Merchants
8500 Briar Wood Blvd
Knoxville, Tennessee 37923

(615) 693-5441

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OCT 14 1986
Office of the Chairman

October 3, 1986

Mr. John Bohn, President
Export-Import Bank of the United States
811 Vermont Avenue, NW
Washington, DC 20571

Dear Mr. Bohn:

We want to thank you again for including our firm in the Ex-Im annual report. The Working Capital Guarantee program has enabled us to greatly expand our small business and we are honored to be used as an example of its success.

During this past year the Ex-Im Guarantee of $450,000 on our $500,000 line was directly responsible for our export sales of about $1,600,000. The line was completely cleaned up at the end of August and we will begin drawing again at the first of October. However this season, due to the continued support of Ex-Im, we anticipate increased sales of an additional $400,000 for total export sales of $2,000,000. This confidence in our sales volume has enabled us to construct a new office/shop facility and increase our full-time employment from 6 to 11 people. The five new employees were added in such basic jobs as truck drivers, mechanics, and timber cutters.

Where this expansion may seem small by some standards it is something we are very proud of. Our firm has survived some very tough times in its own industry as well as world and dollar related problems. Now we are prepared to take advantage of the opportunities that present themselves to us.

If we can be of assistance in any manner, call on us as needed. You have a good program that works. Our firm wouldn't be in existance without it and we will gladly explain it to anyone.

Sincerely,

Victor Jernigan

Victor Jernigan
Owner

"There's no reason in the world why you can't have a banking relationship where both people smile."

Marc Villa, President
North Atlantic Timber and Shipping Company

Not many exporters are smiling these days. With the volatility of the dollar, [illegible] federal regulations, strong foreign competition, and communication difficulties, exporting is a difficult business. In the capital-intensive [illegible] timber industry, exporting [illegible] impossible.

But [illegible] smiling [illegible] Marc Villa.

He [illegible] as a way to [illegible] the U.S. and provide [illegible] at Hardwick, Massachusetts. Marc knew he would be able to [illegible] substantial [illegible] substantially [illegible].

The [illegible] his own vessel up to 500 trailer truck loads a year. And that required [illegible] financing. That's when BayBanks came in.

Throughout his years of export experience, Marc had several banking relationships. He was anxious to find the right financial partner to help him build his fleet and his business. He found BayBanks believed in close long-term relationships as well. And BayBanks believed in him.

Officers from BayBanks worked closely with several government agencies, including the Massachusetts Industrial Finance Agency, to secure a grant for the fleet. Taking advantage of the [illegible] program offered by the Export-Import Bank of the United States, BayBanks helped develop an asset-based credit facility which provides working capital for North Atlantic.

BayBanks has also used other government programs that enable North Atlantic to acquire inventory and [illegible] accounts receivable. Under [illegible] working capital guarantee, BayBanks finances Marc's timber purchases. The guarantee is one of only [illegible] banks granted since the program's inception. The company's [illegible] accounts receivable are insured against commercial and political risk under an insurance policy issued by the Foreign Credit Insurance Association, a [illegible] arm of Eximbank.

To keep on top of Marc's fast-paced, complicated business, an attentive, innovative banker is especially important. At BayBanks, Marc has one.

He depends on BayBanks experts who specialize in asset-based lending, money market investments, cash management, and international finance. All coordinated by one Corporate Financial Officer who follows North Atlantic's local, federal, and international transactions from Hardwick to Hong Kong.

So why is this man smiling? Because his customers are. Because his employees are. And that means at BayBanks, [illegible].

You know BayBanks [illegible] personal banking [illegible]. You'll find our [illegible] billion corporate financial network [illegible] New England business [illegible]. Ask Marc Villa. Or [illegible] other corporate customers.

"My European customers like to develop real relationships, a bond. I was hoping to find the same in a banker."

"My banker knows what color socks I'm wearing and exactly what's going on in my business. For the first time in my banking relationships, I'm content."

BayBanks

Corporate Banking Network

PREPARED STATEMENT OF JOHN R. COX, ACTING ASSOCIATE DEPUTY ADMINISTRATOR FOR SPECIAL PROGRAMS, U.S. SMALL BUSINESS ADMINISTRATION

MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE:

I APPRECIATE THE OPPORTUNITY TO APPEAR BEFORE THE SMALL BUSINESS COMMITTEE TODAY TO DISCUSS THE SMALL BUSINESS ADMINISTRATION'S EFFORTS TO ASSIST SMALL BUSINESS IN THE INTERNATIONAL TRADE AREA.

WITH ME TODAY IS MR. EDWIN HOLLOWAY, ASSOCIATE ADMINISTRATOR FOR FINANCE AND INVESTMENT, MS. JOHNNIE ALBERTSON, DEPUTY ASSOCIATE ADMINISTRATOR, OFFICE OF SMALL BUSINESS DEVELOPMENT CENTERS, AND MICHAEL DEEGAN, DIRECTOR OFFICE OF INTERNATIONAL TRADE.

THE OFFICE OF INTERNATIONAL TRADE WAS LEGISLATIVELY ESTABLISHED AND ASSIGNED SPECIFIC PROGRAMS AND TASKS IN SECTION III OF PUBLIC LAW 96-481, COMMONLY REFERRED TO AS THE "SMALL BUSINESS EXPORT EXPANSION ACT OF 1980."

IN ADDITION TO AUTHORIZING THE AGENCY TO ESTABLISH AN EXPORT REVOLVING LINE OF CREDIT PROGRAM, THE LAW DIRECTS THE AGENCY TO "... PROMOTE SALES OPPORTUNITIES FOR SMALL BUSINESS GOODS AND SERVICES ABROAD" BY:

1. PROVIDING "SMALL BUSINESSES WITH ACCESS TO CURRENT AND COMPLETE INFORMATION" ON EXPORTING;

2. ENCOURAGING ... "GREATER SMALL BUSINESS PARTICIPATION IN TRADE FAIRS, SHOWS, MISSIONS, AND OTHER DOMESTIC AND OVERSEAS EXPORT DEVELOPMENT ACTIVITIES OF THE DEPARTMENT OF COMMERCE;" AND

3. "FACILITATING "DECENTRALIZED DELIVERY OF EXPORT INFORMATION AND ASSISTANCE TO SMALL BUSINESSES...".

SINCE PL 96-481 WAS ENACTED, THE AGENCY HAS UNDERTAKEN TO IMPLEMENT THE INTENT OF CONGRESS AS OUTLINED IN THAT LEGISLATION AND WITHIN THE CONTENT OF OTHER LEGISLATION ENACTED BY THE CONGRESS WHICH AFFECT THE SMALL BUSINESS ADMINISTRATION.

THROUGH A STAFF IN WASHINGTON, REGIONAL INTERNATIONAL TRADE OFFICERS IN OUR TEN REGIONAL OFFICES, AND DESIGNATED PERSONS IN OUR DISTRICT OFFICES, WE ARE WORKING WITHIN THE INTERNATIONAL TRADE NETWORK OF FEDERAL, STATE AND LOCAL PRIVATE AND PUBLIC SECTOR ORGANIZATIONS TO HELP BROADEN THE NATION'S BASE OF SUCCESSFUL SMALL BUSINESS EXPORTERS.

THIS COMMITTEE, MR. CHAIRMAN, HAS NOTED IN VARIOUS REPORTS THAT:

> SMALL FIRMS ARE VERY OFTEN RELUCTANT TO EXPLORE FOREIGN MARKETS AS A SOURCE OF ADDITIONAL SALES. THE RELUCTANCE STEMS FROM NOT KNOWING WHERE TO FIND WHICH COUNTRIES WHO MAY WANT TO BUY THEIR PRODUCTS AND OTHER SERVICES THEY PRODUCE. THEY DO NOT KNOW HOW TO GO ABOUT OBTAINING ASSISTANCE OR CONSOLIDATING THE VAST AMOUNT OF INFORMATION THAT IS ACTUALLY AVAILABLE.

IN SURVEYS CONDUCTED BY THE SBA, THE NATIONAL FEDERATION OF INDEPENDENT BUSINESS, THE SENATE SMALL BUSINESS COMMITTEE, THE CHAMBER OF COMMERCE OF THE UNITED STATES, AND OTHER ORGANIZATIONS, INDICATED A LACK OF INFORMATION ON (1) WHERE MARKETS EXIST FOR THEIR PRODUCTS OR SERVICES, AND (2) THE PROCEDURES TO BE FOLLOWED IN SUCCESSFULLY COMPLETING POTENTIAL SALES WITHIN THESE MARKETS, TOGETHER WITH ACCESS TO REQUISITE FINANCING WERE GENERIC PROBLEMS FOR THE POTENTIAL SMALL BUSINESS EXPORTER.

FOSTERING AND ENCOURAGING INCREASED EXPORTS FROM THE UNITED STATES IS THE PRIME RESPONSIBILITY OF THE U. S. DEPARTMENT OF COMMERCE, INTERNATIONAL TRADE ADMINISTRATION -- PARTICULARLY IN THE AREAS OF MARKET IDENTIFICATION, INFORMATION COLLECTION AND DISSEMINATION, AND ASSISTING AMERICAN COMPANIES IN ACCOMPLISHING THEIR BUSINESS OBJECTIVES IN TARGETED COUNTRIES THROUGH VARIOUS TRADE PROMOTION ACTIVITIES.

THE SMALL BUSINESS ADMINISTRATION IS REQUIRED BY STATUTE AND ADMINISTRATION MANDATE TO AID, COUNSEL, AND ASSIST SMALL BUSINESSES IN THE VERY BROADEST OF TERMS THROUGH SEVERAL PROGRAMS. OUR INTERNATIONAL TRADE-RELATED RESPONSIBILITIES REVOLVE PRIMARILY UPON WORKING, IN A SUPPORTIVE ROLE, WITH OTHER FEDERAL AGENCIES AND PRIVATE SECTOR ORGANIZATIONS CONCERNED WITH INTERNATIONAL TRADE AND INVESTMENT.

WE RECOGNIZE THAT THERE ARE MANY ORGANIZATIONS WITHIN THE PUBLIC AND PRIVATE SECTORS THAT ARE INVOLVED IN INTERNATIONAL TRADE. WE SHARE THE SAME OBJECTIVES TO INCREASE THE COMPETITIVE POSITION OF AMERICAN BUSINESS IN THE WORLD MARKETPLACE. BY WORKING TOGETHER IN THIS EFFORT, THE SMALL BUSINESS COMMUNITY WILL GROW AND PROSPER, CREATE MORE JOBS AND FOSTER INNOVATION WHICH HAS BEEN THE HALLMARK OF THE AMERICAN FREE ENTERPRISE SYSTEM.

IT IS FOR THIS REASON THAT DURING FY 1987, OUR MAJOR FOCUS IN INTERNATIONAL TRADE IS TO WORK WITH OTHER ORGANIZATIONS AT THE STATE AND LOCAL LEVEL TO IDENTIFY THE NEEDS OF THE SMALL BUSINESS AS THEY PERTAIN TO EXPORTING AND JOINTLY PLAN ACTIVITIES DESIGNED TO MEET THOSE NEEDS.

WE ARE ENCOURAGING OUR DISTRICT OFFICES TO BECOME MEMBERS OF LOCAL WORLD TRADE ORGANIZATIONS AND DEPARTMENT OF COMMERCE DISTRICT EXPORT COUNCILS IN ORDER TO BECOME AWARE OF AND PARTICIPATE IN THEIR ACTIVITIES WHERE APPROPRIATE.

THE SMALL BUSINESS ADMINISTRATION AND THE DEPARTMENT OF COMMERCE ARE IN THE PROCESS OF REVISING OUR CURRENT MEMORANDUM OF UNDERSTANDING TO ENCOURAGE GREATER COOPERATION AND JOINT PLANNING AT ALL LEVELS AND THEREBY BETTER SERVE THE SMALL BUSINESS COMMUNITY.

OUR DISTRICT OFFICES HAVE BEEN INSTRUCTED TO HAVE AVAILABLE LOCAL DIRECTORIES OF EXPORT ASSISTANCE PROGRAMS AND SERVICES IN ORDER THAT THEY CAN REFER SMALL BUSINESSES TO THEM FOR ADVICE AND COUNSEL.

DURING FY 1987, WE WILL BE INCREASING OUR EFFORTS ON GREATER OUTREACH TO THE SMALL BUSINESS COMMUNITY TO IDENTIFY THOSE SMALL BUSINESSES WITH EXPORT POTENTIAL AND INTEREST.

OUR PROCUREMENT AUTOMATED SOURCE SYSTEM (PASS) HAS IDENTIFIED OVER 50,000 SMALL FIRMS THAT HAVE AN INTEREST IN EXPORTING. WE WILL BE REACHING OUT TO THESE FIRMS MAKING THEM AWARE OF THE VARIOUS SERVICES AVAILABLE TO THEM.

WE INTEND TO SHARE THIS DATA BASE WITH STATE AND LOCAL GOVERNMENT OFFICIALS, AS WELL AS OUR SISTER FEDERAL AGENCIES, IN ORDER THAT MORE SMALL BUSINESSES CAN BECOME AWARE OF WHAT ADDITIONAL SERVICES ARE AVAILABLE TO HELP THEM SUCCESSFULLY UNDERTAKE EXPORT OPERATIONS.

I WOULD LIKE TO BRIEFLY DESCRIBE THE INTERNATIONAL TRADE ASSISTANCE AVAILABLE TO SMALL BUSINESS FIRMS FROM THE SMALL BUSINESS ADMINISTRATION. THESE PROGRAMS ARE AVAILABLE THROUGH OUR NETWORK OF OVER 100 OFFICES ACROSS THE COUNTRY.

EXPORT COUNSELING

BASIC COUNSELING CONCERNING HOW TO IDENTIFY MARKETS AND ESTABLISH AND CONDUCT EXPORT OPERATIONS IS OFFERED BY BUSINESS EXECUTIVES EXPERIENCED IN INTERNATIONAL TRADE WHO HAVE RETIRED FROM OR WHO ARE STILL ENGAGED IN INTERNATIONAL TRADE.

THESE VOLUNTEERS FROM THE SERVICE CORPS OF RETIRED EXECUTIVES (SCORE) AND THE ACTIVE CORPS OF EXECUTIVES (ACE) PROGRAMS, BASED UPON THEIR MANY YEARS OF EXPERIENCE IN INTERNATIONAL TRADE, COUNSEL THE CURRENT OR PROSPECTIVE SMALL BUSINESS EXPORTER.

EACH SBA DISTRICT OFFICE AND SCORE CHAPTER IS DEDICATED TO RECRUITING ADDITIONAL COUNSELORS AND DEVELOPING COUNSELING TEAMS AS NEEDED TO INITIALLY CONTACT POTENTIAL SMALL EXPORTERS AND PROVIDE THEM WITH BASIC COUNSELING AND TRAINING. FIRMS ARE THEN REFERRED TO OTHER PUBLIC AND PRIVATE SECTOR ORGANIZATIONS FOR MORE INDEPTH ASSISTANCE.

IN AN EFFORT TO MAKE SCORE COUNSELING MORE ACCESSIBLE TO SMALL BUSINESSES, COUNSELORS OPERATE OUT OF SOME INTERNATIONAL TRADE ADMINISTRATION'S OFFICES AS WELL AS CHAMBERS OF COMMERCE.

MORE INDEPTH MARKET RESEARCH AND ASSISTANCE IS AVAILABLE THROUGH THE SMALL BUSINESS INSTITUTE'S UNIVERSITY-BASED PROGRAM. THIS PROGRAM INVOLVES GRADUATE AND SENIOR UNDERGRADUATE BUSINESS STUDENTS UNDER THE DIRECTION OF FACULTY. INTERNATIONAL TRADE COUNSELING IS ALSO AVAILABLE THROUGH SMALL BUSINESS DEVELOPMENT CENTERS (SBDC).

SOME SMALL BUSINESS DEVELOPMENT CENTERS ARE MORE ACTIVE IN INTERNATIONAL TRADE THAN OTHERS. THE UNIVERSITY OF GEORGIA, THE UNIVERSITY OF ALABAMA AND THE WASHINGTON STATE UNIVERSITY, AMONG OTHERS, HAVE ESTABLISHED SEPARATE INTERNATIONAL TRADE DEVELOPMENT CENTERS WHICH ARE STAFFED BY FULL-TIME PROFESSIONALS, AS WELL AS STUDENTS MAJORING IN INTERNATIONAL BUSINESS. THEY PERFORM MARKET RESEARCH FOR LOCAL SMALL BUSINESSES, PUBLISH INTERNATIONAL TRADE NEWSLETTERS AND ORGANIZE LOCAL SMALL BUSINESS PARTICIPATION IN OVERSEAS EXPORT PROMOTION EVENTS. THEY ALSO WORK WITH THEIR STATE DEPARTMENTS OF COMMERCE AND ECONOMIC DEVELOPMENT TO ENCOURAGE FOREIGN INVESTMENT IN THEIR STATES.

IN ADDITION, OVER THE PAST SEVERAL YEARS, THE UNIVERSITY OF GEORGIA, SMALL BUSINESS DEVELOPMENT CENTER, HAS OPERATED AN EXPORT INFORMATION SYSTEM (XIS) FOR THE AGENCY. THE XIS REPORT IS DESIGNED TO ANSWER THE BASIC QUESTION A SMALL, WOULD-BE EXPORTER WILL ASK: "WHERE MIGHT THERE BE A MARKET OVERSEAS FOR PRODUCTS SIMILAR TO MINE?"

BASED UPON DATA DEVELOPED BY THE UNITED NATIONS CONCERNING WORLD IMPORTS BY MEMBER NATIONS OF OVER 2,700 PRODUCTS, THESE XIS REPORTS TRACK 5-YEAR IMPORT TRENDS AND IDENTIFY THOSE MARKETS WHICH HAVE THE MOST SIGNIFICANT DOLLAR AMOUNT AND MARKET SHARE OF U. S. IMPORTS.

SINCE THE INFORMATION IS ON A MACRO-BASIS, WE URGE FIRMS TO GET MORE SPECIFIC, UP-TO-DATE MARKET INFORMATION FROM ITA OR STATE EXPORT DEVELOPMENT OFFICES.

UNDER AN AGREEMENT BETWEEN THE SMALL BUSINESS ADMINISTRATION AND THE FEDERAL BAR ASSOCIATION (FBA), A SMALL FIRM NOW CAN RECEIVE AN INITIAL, FREE CONSULTATION WITH AN ATTORNEY TO DISCUSS LEGAL ISSUES AND CONCERNS RELATING TO INTERNATIONAL TRADE. A LOCAL FBA/SBA COORDINATOR HAS BEEN APPOINTED IN MAJOR CITIES ACROSS THE COUNTRY.

IN ADDITION, THE FBA HAS PROVIDED TO SBA A HANDBOOK ENTITLED, "LEGAL ASPECTS OF EXPORTING: AN INTRODUCTION" WHICH DISCUSSES VARIOUS LEGAL ISSUES INVOLVED IN INTERNATIONAL TRADE. COPIES HAVE BEEN DISTRIBUTED TO SBA OFFICES AROUND THE COUNTRY.

DURING FY 1986, EXPORT-IMPORT COUNSELING WAS PROVIDED THROUGH THESE RESOURCES TO OVER 3,500 CLIENTS.

EXPORT TRAINING

DISTRICT OFFICES OF THE SMALL BUSINESS ADMINISTRATION COSPONSOR EXPORT TRAINING SEMINARS AND WORKSHOPS WITH THE U. S. DEPARTMENT OF COMMERCE AND OTHERS INTERESTED IN INTERNATIONAL TRADE. THESE TRAINING PROGRAMS EMPHASIZE THE PRACTICAL APPLICATION OF SUCCESSFUL EXPORTING PROCEDURES TO SMALL BUSINESS.

TRAINING PROGRAMS ARE ALSO CONDUCTED BY SCORE/ACE VOLUNTEERS, SMALL BUSINESS DEVELOPMENT CENTERS, OTHER UNIVERSITIES AND JUNIOR COLLEGES, AS WELL AS PRIVATE SECTOR ENTITIES.

IN FY 86, 419 SUCH PROGRAMS ATTENDED BY OVER 17,000 PERSONS WERE HELD.

IN FY 87, WE INTEND TO BECOME MORE INVOLVED WITH PRIVATE SECTOR ORGANIZATIONS INCLUDING FOR-PROFIT CORPORATIONS, AS WELL AS FEDERAL, STATE AND LOCAL GOVERNMENTS, IN SUPPORTING OUTREACH PROGRAMS SUCH AS CONFERENCES, SEMINARS, AND WORKSHOPS WHICH IDENTIFY POTENTIAL SMALL BUSINESS EXPORTERS AND PROVIDE LINKAGES TO NEEDED INFORMATION AND ASSISTANCE.

AS PART OF THIS EFFORT, WE ARE COSPONSORING WITH THE U. S. AGENCY FOR INTERNATIONAL DEVELOPMENT (AID) A SERIES OF FOUR ONE-DAY "OPPORTUNITIES FOR INTERNATIONAL BUSINESS CONFERENCES." THESE PROGRAMS ARE DESIGNED TO INCREASE THE OPPORTUNITY FOR SMALL BUSINESSES TO PARTICIPATE IN AID PROGRAMS.

IN ADDITION, THE AGENCY WILL COSPONSOR WITH THE EXPORT-IMPORT BANK A SERIES OF OUTREACH CONFERENCES TO BE HELD AROUND THE COUNTRY TO EXPLAIN TO THE SMALL BUSINESS EXPORTING COMMUNITY EXIM'S NEW FINANCING PROGRAMS.

EXPORT PROMOTION EVENTS

BEGINNING IN THE FALL OF 1982 THROUGH JUNE 1986, THROUGH MEMORANDA OF UNDERSTANDING WITH THE INTERNATIONAL TRADE ADMINISTRATION, THE NATIONAL MARINE FISHERIES SERVICE OF THE DEPARTMENT OF COMMERCE AND THE FOREIGN AGRICULTURAL SERVICE, SBA AGREED TO SUPPORT THE PARTICIPATION OF 241 SMALL BUSINESSES IN 30 EXPORT PROMOTION EVENTS SUCH AS TRADE SHOWS AND TRADE MISSIONS.

THESE SHOWS AND MISSIONS HAVE TAKEN PLACE PRIMARILY IN THE DEVELOPED COUNTRIES OF EUROPE AND THE PACIFIC RIM.

THESE EVENTS HAVE BEEN BENEFICIAL TO THOSE BUSINESSES THAT PARTICIPATED. HOWEVER, THIS TYPE OF ACTIVITY HAS HAD MINIMAL IMPACT WHEN CONSIDERING THE SCOPE OF ASSISTANCE THAT IS NEEDED BY THE SMALL BUSINESS COMMUNITY IN THE INTERNATIONAL TRADE AREA. IN ADDITION, TRADE MISSION SUPPORT IS BEING PROVIDED BY THE PRIVATE SECTOR AND WE FEEL THAT WE CAN BETTER SERVE THE SMALL BUSINESS COMMUNITY BY MAKING THEM AWARE OF THESE PRIVATE SECTOR PROGRAMS AND THOSE OF OTHER AGENCIES AT THE FEDERAL, STATE AND LOCAL LEVEL. WE ARE RECEPTIVE TO ASSISTING OTHER FEDERAL AGENCIES BY SUPPORTING SMALL BUSINESS PARTICIPATION IN PROMOTION EVENTS TO BE HELD IN THOSE AREAS OF THE WORLD THAT HAVE UNTAPPED POTENTIAL.

EXPORT FINANCING

EXPORTERS MAY OBTAIN FUNDS FOP FIXED ASSET ACQUISITION NECESSARY FOR BUSINESS START-UP OR EXPANSION AND FOR OTHER GENERAL WORKING CAPITAL PURPOSES THROUGH SBA's REGULAR 7(a) BUSINESS LOAN GUARANTEE PROGRAM. THEY MAY ALSO OBTAIN FUNDS FOR FIXED ASSET FINANCING THROUGH THE 504 CERTIFIED DEVELOPMENT COMPANY PROGRAM. LOAN GUARANTEES FOR FIXED ASSET ACQUISITION HAVE A MAXIMUN MATURITY OF 25 YEARS. GUARANTEES FOR GENERAL PURPOSES, TERM WORKING CAPITAL LOANS ARE USUALLY LIMITED TO A MAXIMUM MATURITY OF 7 YEARS.

BUSINESSES FINANCED BY SMALL BUSINESS INVESTMENT COMPANIES (SBIC'S) ARE SOMETIMES ENGAGED IN EXPORTING. SBIC'S WERE INVOLVED IN VERY EARLY VENTURE CAPITAL FINANCING OF COMPANIES LIKE APPLE COMPUTER, ROLM, INTEL AND CRAY RESEARCH WHICH ARE OR HAVE BEEN MAJOR EXPORTERS.

IN ORDER TO HELP MORE SMALL BUSINESSES EXPORT THEIR PRODUCTS AND SERVICES ABROAD, THE CONGRESS AND SBA ESTABLISHED THE EXPORT REVOLVING LINE OF CREDIT LOAN GUARANTY PROGRAM (ERLC) SPECIFICALLY FOR ELIGIBLE SMALL BUSINESS EXPORTERS.

UNDER THIS PROGRAM, SBA CAN GUARANTEE UP TO 90% OR $500,000 OF A SHORT-TERM BANK LINE OF CREDIT FOR WORKING CAPITAL PURPOSES. LOAN PROCEEDS MAY ONLY BE USED TO FINANCE LABOR AND MATERIALS FOR PRE-EXPORT PRODUCTION AND TO PENETRATE OR DEVELOP FOREIGN MARKETS. THE SPECIFIC MATURITY OF AN ERLC IS BASED ON A BORROWER'S BUSINESS CYCLE BUT CANNOT EXCEED 18 MONTHS. DURING THE MATURITY PERIOD, ANY NUMBER OF WITHDRAWALS AND REPAYMENTS CAN BE MADE AS LONG AS THE DOLLAR LIMIT OF THE LINE IS NOT EXCEEDED.

IN ADDITION, THE SBA AND THE EXPORT-IMPORT BANK OF THE UNITED STATES CAN JOINTLY GUARANTY WORKING CAPITAL LOANS BETWEEN $200,000 AND $1,000,000 WITHIN THE FRAMEWORK OF THE EXPORT REVOLVING LINE OF CREDIT PROGRAM PREVIOUSLY DESCRIBED.

IF AN EXPORTING COMPANY REQUIRED ADDITIONAL EQUITY CAPITAL OR AMOUNTS OF TERM WORKING CAPITAL IN EXCESS OF SBA'S $500,000 STATUTORY MAXIMUM, A SMALL BUSINESS INVESTMENT COMPANY (SBIC), APPROVED AND LICENSED BY THE SBA, MAY BE ABLE TO PROVIDE THE NECESSARY FUNDING, DEPENDING UPON WHETHER THE SBIC's INVESTMENT STRATEGY INCLUDES SUCH ACTIVITIES.

DESPITE EXTENSIVE EFFORTS TO ADIVSE BANKS OF THE AVAILABILITY OF SBA PROGRAMS TO PROVIDE FINANCING TO SMALL EXPORTERS THROUGH DIRECT MAILINGS TO EVERY BANK IN THE COUNTRY, BRIEFINGS TO ASSEMBLED GROUPS OF BANKERS, MEETINGS WITH INDIVIDUAL BANK LOAN OFFICERS, AND COVERAGE OF OUR PROGRAMS IN EXPORT COUNSELING AND TRAINING ACTIVITIES, UTILIZATION OF OUR PROGRAMS HAS NOT BEEN EXTENSIVE. SINCE THE EXPORT REVOLVING LINE OF CREDIT PROGRAM BECAME AVAILABLE IN 1983, 87 SUCH LOANS HAVE BEEN APPROVED TOTALING $23.5 million.

THIS LOW LEVEL OF ACTIVITY MAY BE DUE IN PART TO A COMBINATION OF REASONS:

1. THE INCREASE IN THE VALUE OF THE U. S. DOLLAR WHICH MADE U. S. EXPORTS LESS COMPETITIVE IN WORLD MARKETS RESULTED IN INCREASINGLY LARGE TRADE DEFICITS AND LOST SALES OPPORTUNITIES FOR SMALL EXPORTERS;

2. THE OVERALL RETRENCHMENT IN BANK LENDING AWAY FROM TRADITIONAL TRADE FINANCING PARTICULARLY BY LARGER MONEY CENTER BANKS;

3. A RESTRUCTURING OF BANK ACTIVITY TOWARD MORE PROFITABLE OPERATIONS WHICH MINIMIZE LENDER RISK AND MAXIMIZE RETURN ON ASSETS AND CAPITAL;

4. A TENDENCY OF INTERNATIONAL DEPARTMENTS OF BANKS TO CONCENTRATE ON LARGER VALUE TRANSACTIONS RATHER THAN SMALL TRANSACTIONS WHICH REQUIRE MORE SERVICING AND RESULTANT OVERHEAD EXPENSES AND PROVIDE A LESSER RATE OF RETURN ON CAPITAL;

5. UNFAMILARITY WITH SBA PROGRAMS BY THE INTERNATIONAL DEPARTMENTS OF BANKS;

6. THE RELATIVE LACK OF EXPORT FINANCING EXPERTISE BY SMALLER BANKS WHICH ARE THE TRADITIONAL SOURCES OF SMALL BUSINESS FINANCING;

7. THE FACT THAT BANKS REGULARLY MAKE SHORT TERM REVOLVING LINE OF CREDIT LOANS ON THEIR OWN, THEREBY REDUCING THE NEED FOR AN SBA GUARANTY. IN CONTRAST, ONE REASON WHY THE SBA GUARANTY IS SO WIDELY USED IN LONG-TERM FINANCING FOR SMALL BUSINESSES IS THAT BANKS ARE NOT LONG-TERM LENDERS; THE SBA GUARANTY THEREFORE OCCUPIES A SPECIAL NICHE IN LONG-TERM FINANCING THAT IT DOES NOT OCCUPY IN SHORT-TERM FINANCING.

8. A CONCERN ABOUT THE CONTINUATION OF THE SMALL BUSINESS ADMINISTRATION'S PROGRAMS.

LET ME ASSURE YOU, MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE, THAT SBA WILL CONTINUE OUR EFFORTS TO ENCOURAGE BANKS TO PROVIDE SMALL BUSINESSES THE EXPORT FINANCING THEY NEED THROUGH WHATEVER PROGRAMS ARE APPROPRIATE. WE ARE EXPLORING WAYS IN WHICH SBA MIGHT COOPERATE MORE EFFECTIVELY WITH STATE EXPORT FINANCING FACILITIES AND WE WELCOME SUGGESTIONS FROM THE COMMITTEE AS TO HOW THIS MIGHT BE ACCOMPLISHED.

WE BELIEVE THAT THE FUNDAMENTAL QUESTIONS THAT YOU IN THE CONGRESS, WE IN THE EXECUTIVE BRANCH, AND OTHERS IN THE PUBLIC AND PRIVATE SECTOR ARE STRUGGLING WITH ARE: (1) WHAT ARE THE NEEDS OF THE SMALL BUSINESS EXPORTER; AND (2) WHAT MIGHT BE DONE THROUGH A COST-EFFECTIVE, PUBLIC-PRIVATE SECTOR PARTNERSHIP, THAT CAN INCREASE THE COMPETITIVENESS OF SMALL BUSINESS IN THE INTERNATIONAL MARKETPLACE?

WE WISH THAT WE HAD THE TOTAL ANSWER . . . BUT WE DON'T.

SBA IS REASSESSING OUR INTERNATIONAL TRADE INVOLVEMENT. ON MARCH 24th, AGENCY PERSONNEL WILL BE MEETING WITH MEMBERS OF THE NATIONAL ADVISORY COUNCIL'S COMMITTEE ON INTERNATIONAL TRADE. WE HAVE INVITED THE STAFF OF THE SMALL BUSINESS COMMITTEES OF BOTH HOUSES. THE PURPOSE OF THIS MEETING IS TO CRITIQUE OUR EXISTING PROGRAMS, FIND OUT WHY THE DEMAND FOR ASSISTANCE HAS DECLINED AND WHAT CAN BE DONE TO REGENERATE INTEREST IN THE INTERNATIONAL TRADE AREA.

WE KNOW OF NO RELIABLE FIGURES ON THE EXTENT OF SMALL BUSINESS EXPORT ACTIVITY AND PARTICULARLY WHICH INDUSTRIES OFFER THE GREATEST EXPORT POTENTIAL FOR SMALL BUSINESS.

THE OFFICE OF ADVOCACY IS IN THE PROCESS OF EVALUATING RECENTLY RECEIVED PROPOSALS THAT WOULD ATTEMPT TO GATHER THIS INFORMATION. THE RESULTANT RESEARCH, WE HOPE, WILL PROVIDE SIGNIFICANT GUIDANCE TO THOSE THAT ARE IN NEED OF THIS TYPE OF INFORMATION.

IT WOULD BE EASY AT THIS POINT, TO SAY, THAT MORE MONEY OR MORE PERSONNEL WOULD REAP LARGE DIVIDENDS BUT WE DO NOT BELIEVE THIS IS THE CASE.

WE BELIEVE THAT IF SBA IS GOING TO HAVE MEANINGFUL IMPACT IN THE INTERNATIONAL TRADE AREA, IT WILL BE IN THE AREA OF INFORMATION DISSEMINATION AND EDUCATION SUPPORT THROUGH OUTREACH PROGRAMS.

IN A MEETING JUST LAST WEEK WITH THE EXECUTIVE BOARD OF THE SERVICE CORPS OF RETIRED EXECUTIVES (SCORE), THAT ORGANIZATION PLEDGED THEIR SUPPORT IN DELIVERING WHATEVER COUNSELING OR TRAINING SERVICES THAT ARE NEEDED.

WE FEEL CONFIDENT THAT THE FOR-PROFIT PRIVATE SECTOR WILL RESPOND, AS THEY HAVE IN THE PAST, IN SUPPORTING EDUCATIONAL PROGRAMS THROUGH CO-SPONSORSHIP AGREEMENTS WITH SBA.

BEFORE WE SPEND LARGE SUMS OF MONEY, BEFORE WE MAKE DECISIONS ON THE NUMBER OF PERSONNEL NEEDED, WE WOULD HOPE THAT WE WOULD HAVE A CLEAR UNDERSTANDING OF WHAT SMALL BUSINESS REALLY NEEDS TO ENTER THE INTERNATIONAL TRADE ARENA AND WHAT ROLE THIS AGENCY CAN REASONABLY PLAY.

IN THE COMING WEEKS, WE BELIEVE OUR ROLE WILL BECOME MUCH CLEARER.

IN SUMMARY, MR. CHAIRMAN, MAY I SAY THAT SBA WELCOMES THIS COMMITTEE'S COMMENTS ON HOW ANY OF OUR PROGRAMS CAN BE REFINED OR HOW NEW PROGRAMS CAN BE DEVELOPED, WITHIN THE AUTHORITY OF OUR ENABLING LEGISLATION. WE ARE NOT, NOR CAN WE BE, THE SOLE PROVIDER OF EXPORT ASSISTANCE TO SMALL BUSINESS. OUR ROLE IS TO ENSURE SMALL BUSINESS ACCESS TO THE TOOLS OF INTERNATIONAL TRADE BY BEING A COORDINATOR, AND A COMMUNICATOR.

THIS ROLE IS NOT NEW TO US. THE ROLE WE PLAYED IN MAKING THIS COUNTRY AWARE OF THE BENEFITS OF SMALL BUSINESS INCUBATORS WAS NOT ACCOMPLISHED THROUGH EXPENSIVE PROGRAMMING OR LARGE STAFFS . . . IT WAS ACCOMPLISHED THROUGH THE SUPPORT OF FOR-PROFIT ENTITIES, AND INDIVIDUAL ENTREPRENEURS WHO GAVE OF THEIR TIME AND TECHNICAL EXPERTISE ... MAKING INDIVIDUALS AWARE THAT ONLY THEY CAN MAKE A DIFFERENCE.

THANK YOU FOR THE OPPORTUNITY TO APPEAR BEFORE YOU TODAY. THIS CONCLUDES MY FORMAL REMARKS. I WILL BE HAPPY TO RESPOND TO ANY QUESTIONS THAT YOU MIGHT HAVE, MR. CHAIRMAN.

Prepared Statement of Richard J. Shane, Assistant Administrator, Office of Innovation, Research, and Technology, U.S. Small Business Administration

Mr. Chairman and Members of the Committee: It is a pleasure to appear before you and the committee today to express the Administration's thoughts in regard to the Small Business Innovation Development Act of 1982 (P.L. 97-219) and its pertinence to the country's trade and competitiveness position.

At the outset, I would like to express the Administration's, and my personal, appreciation for the continuing interest and support of the Chairman and the Committee. The achievements of the Small Business Innovation Research Program are gratifying in that it is meeting or exceeding the purposes of the legislation. This success is due to the mutual efforts of the Administration, the Small Business Administration, the participating agencies and this Committee. I would like to

MAKE NOTE OF THE FACT THAT THE CHAIRMAN HAS CONTINUED HIS PERSONAL SUPPORT OF THE PROGRAM SINCE ITS INCEPTION.

ON JUNE 17, 1982, THE CHAIRMAN, ACTING AS FLOOR MANAGER PRESENTED TO THE WHOLE HOUSE OF REPRESENTATIVES H.R. 4326, THE SMALL BUSINESS INNOVATION DEVELOPMENT ACT. AT THAT TIME HE STATED "WE CANNOT AFFORD TO LOSE OUR ABILITY TO INNOVATE. IF WE LOSE THAT, WE LOSE OUR ABILITY TO INCREASE U.S. PRODUCTIVITY; WE LOSE OUR ABILITY TO MAINTAIN U.S. TECHNOLOGICAL PREEMINENCE; WE LOSE OUR ABILITY TO CREATE MANY OF THE 20 MILLION NEW JOBS ESSENTIAL FOR A FULL EMPLOYMENT RECOVERY; WE LOSE OUR ABILITY TO COMPETE IN WORLD MARKETS AND WE LOSE OUR ABILITY TO PREVENT PERMANENT DAMAGE TO OUR ECONOMY AND SOCIETY."

MR. CHAIRMAN, YOUR EXPRESSED THOUGHTS THEN REMAIN VALID TODAY AND WE BELIEVE THAT THE SMALL BUSINESS INNOVATION RESEARCH PROGRAM HAS AND WILL CONTINUE TO ASSIST IN THE RESOLUTION OF THESE PROBLEMS.

THE SMALL BUSINESS INNOVATION RESEARCH PROGRAM IS NOW IN ITS FIFTH YEAR OF PERFORMANCE. THIS YEAR IS THE FIRST YEAR THAT ALL OF THE PARTICIPATING ELEVEN AGENCIES BUDGETS HAVE REACHED THE LEGISLATED 1.25 PERCENTUM. WE ARE CURRENTLY COLLECTING AND ANALYZING THE 1986 FISCAL YEAR PROGRAM DATA AND WE WILL SUBMIT

OUR FOURTH ANNUAL SBIR REPORT TO THE CONGRESS THIS SUMMER. EARLY AGENCY DATA INDICATES THAT THERE WERE APPROXIMATELY 13,600 PROPOSALS SUBMITTED. THIS RESULTED IN APPROXIMATELY 1,850 PHASE I AND 650 PHASE II AWARDS IN THE ESTIMATED AMOUNT OF $274 MILLION. I AM PLEASED TO REPORT THAT DURING THIS PROGRAM MATURATION PROCESS THE TECHNICAL QUALITY OF THESE PROPOSALS AND AWARDS HAS REMAINED HIGH.

A PRIMARY PURPOSE OF THE SMALL BUSINESS INNOVATION RESEARCH PROGRAM IS THE COMMERCIALIZATION OF THE RESEARCH. TO ASSIST THIS PROCESS WE HAVE DEVELOPED A COMMERCIALIZATION MATCHING SYSTEM WHICH THROUGH THE USE OF KEYWORD COMPUTER SEARCH PROGRAM SBIR AWARDEES AND POTENTIAL SOURCES OF CAPITAL ARE MATCHED. THE COMPUTER SYSTEM CURRENTLY HAS 4,451 SBIR AWARDEES AND 525 SOURCES OF CAPITAL. AT THE REQUEST OF THE CMS PARTICIPANTS WE HAVE PROCESSED 700 REQUESTS. WE STRONGLY FEEL THIS SYSTEM WILL BE OF CONSIDERABLE ASSISTANCE IN THE COMMERCIALIZATION PROCESS.

THIS YEAR THE SECOND GROUP OF PHASE II AWARDEES REACH PROGRAM COMPLETION. WE LOOK FORWARD TO EVALUATING, OVER THE NEXT THREE YEARS, THE PROGRESS OF THE SBIR DEVELOPED INNOVATIONS. THE NATIONAL AND INTERNATIONAL POTENTIAL MARKETS FOR AMERICA'S HIGH TECHNOLOGY PRODUCTS ARE PRIMARILY BASED UPON THE PERFECTION OF LONG TERM PRODUCTION AND MARKETING PROGRAMS.

THE SBIR PROGRAM CAN HELP IMPROVE THE NATION'S COMPETITIVE POSITION IN TWO WAYS.

FIRST, THE VERY NATURE OF THE LEGISLATION THAT YOU ESTABLISHED FOR THE PROGRAM ASSURES THAT MORE R&D IS UNDERTAKEN BY THE SMALL BUSINESS SECTOR. A FAR MORE EFFICIENT APPROACH THAN OUR PREVIOUS DEPENDENCE ON LARGER BUSINESSES AND NON-PROFITS. THIS LEGISLATION HAS STREAMLINED EVERY ASPECT OF THAT R&D WHICH IS ACCOMPLISHED UNDER IT, WHILE ENCOURAGING THE WORK TO BE DONE BY THOSE WHO EXPECT THESE MAJOR REWARDS TO COME FROM THE COMMERCIALIZATION OF THE PRODUCT AND NOT FROM THE RESEARCH PROCESS ITSELF.

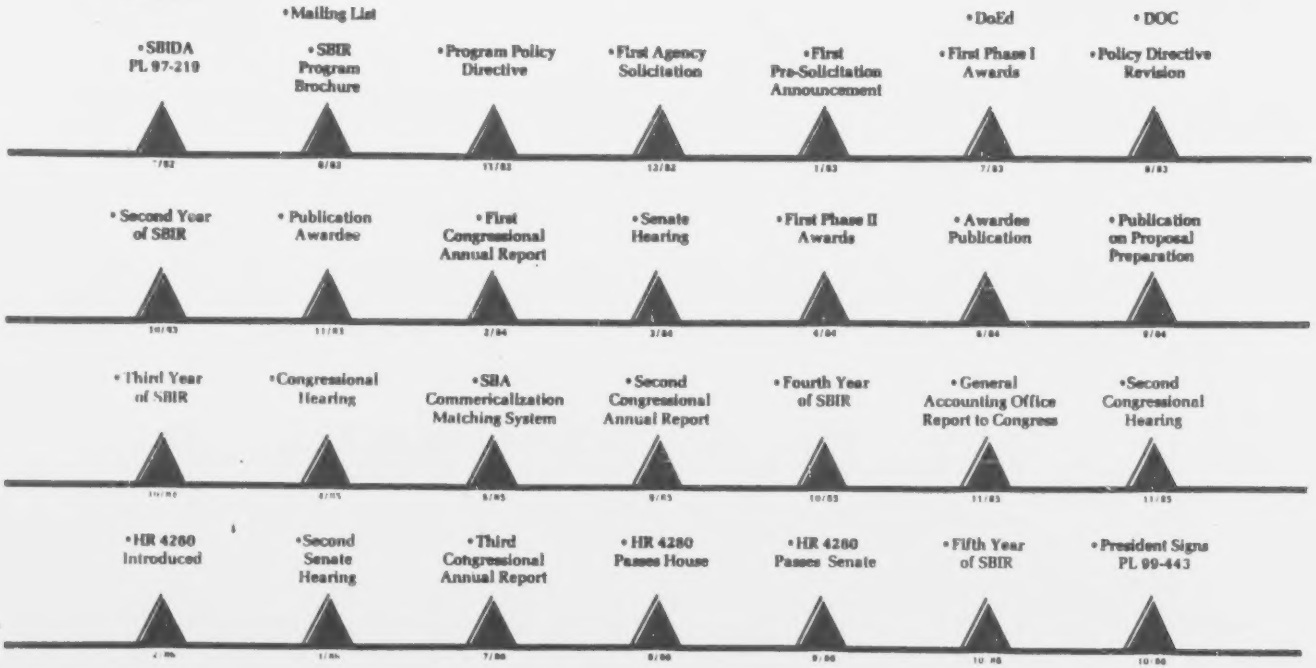
SECOND, THE TREMENDOUS DIVERSITY OF NEW HIGH TECH PRODUCTS AND SERVICES THAT WE ARE CONFIDENT THIS PROGRAM IS PRODUCING, WILL ADD SUBSTANTIALLY TO THE AVAILABILITY OF THESE INNOVATIONS NOT ONLY TO OUR OWN PEOPLE, BUT AVAILABLE FOR EXPORT.

MR. CHAIRMAN: THIS CONCLUDES MY PREPARED STATEMENT. I WILL BE PLEASED TO ANSWER ANY QUESTION THE COMMITTEE MAY HAVE.

U.S. SMALL BUSINESS ADMINISTRATION

Small Business Innovation Research Program

Program Chronology



• SBIDA PL 97-219
7/82

• Mailing List
• SBIR Program Brochure
8/82

• Program Policy Directive
11/82

• First Agency Solicitation
12/82

• First Pre-Solicitation Announcement
1/83

• DoEd
• First Phase I Awards
7/83

• DOC
• Policy Directive Revision
8/83

• Second Year of SBIR
10/83

• Publication Awardee
11/83

• First Congressional Annual Report
2/84

• Senate Hearing
3/84

• First Phase II Awards
4/84

• Awardee Publication
8/84

• Publication on Proposal Preparation
9/84

• Third Year of SBIR
10/84

• Congressional Hearing
4/85

• SBA Commericalization Matching System
5/85

• Second Congressional Annual Report
9/85

• Fourth Year of SBIR
10/85

• General Accounting Office Report to Congress
11/85

• Second Congressional Hearing
11/85

• HR 4260 Introduced
2/86

• Second Senate Hearing
1/86

• Third Congressional Annual Report
7/86

• HR 4260 Passes House
8/86

• HR 4260 Passes Senate
9/86

• Fifth Year of SBIR
10/86

• President Signs PL 99-443
10/86

PREPARED STATEMENT OF BRUCE SMART, UNDER SECRETARY FOR INTERNATIONAL TRADE, U.S. DEPARTMENT OF COMMERCE

Mr. Chairman and members of the Committee:

During my 36 years as a business executive I have been fascinated by the web of enterprise that constitutes the American economy, and how firms of all size interrelate to create the standard of living and industrial preeminence that we now enjoy, and I fear, take for granted almost as an entitlement.

I believe that preeminence is in danger of being lost. To protect it, we need to reawaken America to the need to compete, to adapt, and to win.

The smaller businesses of our nation must play a key role in this effort, as they have in our domestic growth. The sectors of our economy heavily populated by small businesses -- wholesale and retail trades, construction, parts and components manufacture, high technology -- are among our top performers and our most important source of new jobs. We now employ 10 million more people in this country than we did in 1980; small businesses have provided two out of every three of these new jobs.

The features that account for the domestic success of small business can make them winners in international markets as well. Typically small businesses represent:

- New market entrants, often in emerging technologies;
- Specialized manufacturing that requires innovation but that can be efficiently produced on a small scale;
- Enterprises of a local or regional nature;
- Services, including professional and para-professional services;
- Suppliers of components and parts; and
- Marketing and distribution functions.

Many small firms are among the most innovative, creative and adaptive of U.S. enterprises. They flourish best in a growing and vibrant economy. That is why any of the initiatives that the Administration and Congress undertake to improve U.S. competitiveness generally will benefit small business as well.

Moreover, small businesses often profit as second and third tier suppliers when large businesses are successful. For example, a 1983 Boeing study estimated that over 2,300 small businesses supply Boeing with goods and services worth almost $450 million annually.

Export statistics that focus attention on only large companies ignore the role of small firms as our "invisible" exporters, that is, as indirect exporters of goods and services incorporated in the exports of large U.S. companies. These small companies will benefit indirectly from the successes of large U.S. firms in international trade.

But small firms also represent a tremendous pool of potential direct exporters. They can be helped to be more effective direct exporters if we can aid them in overcoming the problems a small company faces in entering a foreign market. Some of these are:

- incomplete market knowledge;
- limited access to local business partners and support services;
- high front end costs;
- inadequate financial resources;
- domestic barriers to efficiency that raise the cost of competing; and
- problems of market access.

THE PRESIDENT'S COMPETITIVENESS INITIATIVE

The President's bill, H.R. 1155, addresses the special needs of small business, as well as the more general concerns of U.S. exporters.

Export Promotion -- Small businesses don't have the resources to develop comprehensive marketing information on their own. The Administration's proposal to establish a national Export Promotion Data System would better integrate information on international sales opportunities to help overcome this gap. For a small fee, this computerized system could answer such business questions as which foreign firms have expressed interest in buying a product, how reliable a particular agent in the United Kingdom may be, or how the market for a specific product is likely to develop in the near future.

Because it uses the Commercial Information Management System (CIMS) as its foundation, the Export Promotion Data System can be up and running during 1987, and can be implemented using existing ITA resources.

Export Trading Companies -- The Export Trading Company Act of 1982 can be an innovative tool for improving the competitiveness of small and medium-sized firms. Export trading companies (ETCs) give small businesses the ability to join forces in overseas markets with protection from antitrust liability under U.S. antitrust laws. Through joint export ventures they can spread the risks of exporting and gain economics of scale that can result in cost reductions.

Small firms hesitant to enter the international arena on their own often participate in joint export activities through their trade associations. We are seeing an increasing trend for these associations to seek antitrust certificates of review to protect themselves and their members.

Moreover, ETCs enable exporters in industries populated by small firms each of whom produces a few products (such as the automobile accessory industry) to present a full line of complementary products to foreign purchasers. This is attractive from the buyer's standpoint and cost effective from the seller's standpoint.

ETCs also offer savings through joint marketing, storage, distribution, and transportation. For example, by participating in a shippers' association, small firms can get the benefits of volume discount transportation rates traditionally available only to large firms.

As good as the ETC Act is, our experience with the program has enabled Commerce to identify areas where the Act can be strengthened. Among other things, the antitrust provisions would unify the current four standards for certification into one concise standard and reinforce the statutory basis for extending protection to members of an applicant. The banking provisions would encourage greater participation by small and regional banks. The current law allows bank ETCs to handle the products of small U.S. manufacturers, but restrictions on profitability and flexibility discourage participation by the small banks most interested in smaller local exporters. These amendments will help the ETC Act achieve its full potential, especially as a marketing tool for small business.

Export Finance -- Competitive export financing can make or break a sale, and small firms have special financing needs. Access to money is often more important than cheap money; their limited borrowing power at banks can constitute an absolute constraint on export operations. Also, many small exporters sell components and need access to shorter-term funds.

While Eximbank serves all segments of the exporting community, roughly 25 percent of its credit finances exports from small businesses. They are seeking to do even better. Eximbank just completed the most significant overhaul of its programs since 1960, a major objective of which was to develop greater access for small and medium-sized exporters with medium sized transactions.

One area where the President's package can make a difference is in combatting unfair foreign competition based on mixed credits. The decision criteria for an international sale should be based on product and performance rather than on distorted financing. Until we can implement an international agreement to limit this practice, we believe it is crucial that Congress appropriate the remaining $200 million in "war chest" funding. This funding can be critical to small businesses who serve as suppliers to major projects as well as to direct exporters. Last year, for example, Eximbank authorized a mixed credit for a $53 million sale of airport navigational equipment by a small engineering firm that otherwise would have lost the sale to a bid backed by a foreign subsidized credit.

Product Liability Insurance -- The top concern voiced at the White House Conference on Small Business was product liability insurance. As these costs have climbed, they have been reflected in higher product prices, making U.S. goods less attractive in both domestic and foreign markets. In addition, high insurance costs have dampened the creativity and risk-taking spirit of small firms, and have even driven some of them out of business altogether.

The Administration proposes solving this problem by reforming our product liability laws. The President's proposal, among other things, returns the system to one based on fault and ensures that a person is responsible only for those damages directly attributed to his proportionate share of fault. This proposal will promote the interests of consumers and protect the free flow of goods by placing reasonable limitations on the excesses of current product liability law.

Foreign Corrupt Practices Act -- We also share the concern of the White House Conference participants about the Foreign Corrupt Practices Act. Uncertainty regarding what practices are prohibited and what practices are permitted under the Act has increased the cost and in some cases discouraged firms from conducting international business. For small businesses without extensive legal departments it is a particular burden.

The Administration proposals would clarify the law, while leaving in place strong sanctions against using bribes to obtain business in foreign countries. Specific reforms include:

- Replacing the "reason to know" standard with a more objective standard, such as "directs or authorizes";
- Specifying the types of payments exempt from the Act; and
- Reforming the Act's burdensome and costly accounting provisions.

Export Controls -- An element of the President's bill that is among the most important responsibilities of the Department of Commerce is improvements in our system of export controls on commercial technologies that may have military uses. We have made significant strides over the past six years in stemming the flow of Western technology to the Soviets, but our procedures at times have unnecessarily hampered U.S. exports.

National security is comprised of both economic vitality and military security. American companies must be healthy and productive if we are to count on them for many of the technological breakthroughs that are so vital to our nation's defense.

Consequently, the President has called for export control reforms that:

1. Decontrol technologies that offer no serious threat to U.S. security.
2. Strengthen controls on truly strategic goods and technologies.
3. Make COCOM procedures uniform and enforcement uniformly rigorous.
4. Strengthen multilateral controls over products and technologies that can contribute to Soviet military capabilities.
5. Eliminate unilateral controls where there is widespread foreign availability.
6. Reduce licensing time by at least one-third, and implement a fair, equitable, and timely dispute-resolution process.
7. Ease high technology trade with the People's Republic of China (PRC).

Consistent with these legislative initiatives, Commerce has already made considerable strides in reducing unnecessary burdens on U.S. industry. Specifically, we have in the past year:

- Reduced average license processing time from 30 days to 20 days; we will meet the President's goal to reduce this further to 14 days;
- Installed a audio response unit that automatically handles requests for Status Checks on Export License Applications ("STELA");

- Raised the processing data rate levels of computers eligible for export under the distribution license program. This change will eliminate over 5,000 individual licenses annually;
- Reduced the paperwork burden on the export community by authorizing a 24-month validity period for individual validated licenses;
- Expanded our export control seminar program, both here and abroad, through our exporter outreach staff; and,
- Established a general license to COCOM countries (G-COM) to authorize exports of some commodities to COCOM countries without an individual validated license. We estimate that the use of G-COM eliminated the need for processing over 12,000 license applications in fiscal year 1986.

These changes will have the greatest impact on small businesses.

A 1977 study by the Office of Management and Budget noted that one out of every four of the most significant industrial innovations since WWII was developed by firms with less than 100 employees, while fully one-half were accounted for by companies with less than 1,000 employees. Propelled by rapid innovation in computers and communications, small business continues to be in the forefront of technological innovation. These firms cannot afford to fly to Washington or to hire law firms to find out about complex regulations and procedures or the status of their export license applications. When small firms do incur these expenses, they represent a proportionately greater burden for them than for large enterprises.

Finally, Commerce has initiated several proposals that cut across all seven of the President's export control initiatives. First, on January 20 controls on exports of non-strategic oil and gas equipment and technology to the Soviet Union were allowed to expire after we determined that they were no longer in the national interest.

Second, in the Federal Register on February 20, we published proposals for two new general licenses that will provide for virtually unrestricted export to government and government-controlled departments, agencies and commercial enterprises at the national level in cooperating countries.

Third, we are developing regulations to eliminate, or at least reduce, reexport controls on items destined for COCOM countries.

Fourth, we have published in the Federal Register proposed regulations to eliminate licensing requirements for certain low-level exports to non-COCOM trading partners in the free world.

Fifth, we are circulating for interagency review regulations that, in many cases, will allow foreign manufacturers to incorporate U.S.-origin parts and components without having to obtain reexport authorization from the U.S. government. This provision should assist our small parts suppliers in selling to large foreign manufacturers. We expect final rules to be published by late March.

IMPROVING THE TRADE ENVIRONMENT

Uruguay Round -- The President's package goes beyond export promotion tools and regulatory reform to improve the international framework in which trade takes place. The Uruguay Round of Multilateral Trade Negotiations, for which the Administration is requesting negotiating authority, is a key forum for expanding trade discipline in areas of importance to small business.

Intellectual Property Rights -- Small business is highly innovative. But these businesses cannot afford to invest in new technology if the fruits of their ingenuity are pirated. The President has made improved intellectual property rights a key U.S. objective in the Uruguay Round.

The President's bill improves domestic IPR protections as well. Among other proposals, small business will have improved access to Section 337 of the Tariff Act of 1930 which protects holders of U.S. rights against infringing imports. The "injury" requirement would be eliminated to make this provision conform to U.S. intellectual property law. Elimination of the "industry" requirement would allow universities and R&D companies to use section 337 to protect their rights.

Services -- Most small businesses are in the service sector, and the fastest growing and most innovative service firms -- business and professional services -- are among those with the most to gain from improved access to international markets. Small business service exports are inhibited by a lopsided international competitive environment. Our services suppliers compete at home against foreign firms whose own markets remain largely closed to U.S. service exports.

In the Uruguay Round, we hope to reach agreement within two years on a framework of principles and rules to govern international services trade. Based on this framework, we will seek to liberalize trade in specific service industries, just as we have done in the case of tariff and non-tariff barriers on specific goods.

Trade Barriers -- More generally, the Uruguay Round offers small business improved GATT rules and procedures and a reduction in foreign trade barriers. For example, procedural changes in the dispute settlement mechanism will aid innovative firms. Because the products of these firms are constantly modified, a delay in the resolution of complaints can cost the competitive advantage for current and future product generations. Another area where we will continue to press for improvements is the Government Procurement

Code. Signatories recently agreed to extend bid submission deadlines, expand coverage to leasing contracts, and reduce the threshold level of coverage -- improvements which should facilitate the entry of smaller producers into this arena.

Trade Laws -- Through the President's Trade Strike Force and the use of self-initiated 301 and antidumping cases, the Administration continues an all-out assault on unfair trade practices. We have had some notable successes -- opening some (but not all!) Japanese markets, gaining appropriate compensation for the trade effects of EC Enlargement, and improving protection of intellectual property rights in Korea.

From our perspective, U.S. trade laws are doing their job for the most part. Nonetheless, some changes are necessary to make our trade laws work even better. We have proposed changes in our antidumping and countervailing duty laws to prevent evasion of duties and to provide a predictable pricing remedy for dumped products from non-market economies; section 301 would be amended to include consideration of reciprocal opportunities in determining if a foreign government practice is unreasonable; and the import remedies available under section 201 would be expanded and made more useful.

COMMERCE PROGRAMS TO ASSIST SMALL BUSINESS

In administering its responsibilities, the Commerce Department already does a number of things intended to meet the special needs of small businesses in international trade.

Small Business Advice -- Officials in the Commerce Department, USTR and other trade agencies meet regularly with the members of the Industry Sector Advisory Committee on Small and Minority Business (ISAC 14). We actively solicit the ISAC's advice on a wide range of issues, and they have suggested numerous initiatives for trade policy and programs. The competitiveness proposals that the Administration has put forward have benefited from the advice and guidance of this group. They offer valuable suggestions on how to improve the delivery of Government services to small business.

Trade Law Assistance -- Small firms require assistance to defend their products from unfair trade practices. The Commerce Department Office of Investigations makes special efforts to assist small firms petitioning for relief under the antidumping and countervailing duty laws. Already this year, 18 small businesses have requested our assistance. In response to letters and telephone calls, often from members of Congress on behalf of their constituents, we provide: 1) a letter that walks firms through the investigation processes; and 2) an information packet containing copies of trade laws, Commerce regulations, and sample questionnaires to guide firms in filing a petition. Upon request, we will send an experienced staff member to company headquarters or meet with company officials in Washington to aid in drafting a petition.

Most recently, this Commerce outreach program resulted in investigations and final orders in antidumping duty cases concerning instrument pads from Italy and neoprene laminate from Japan. A current investigation -- neoprene laminate from Taiwan -- also was initiated as a result of our small business assistance program.

Export Assistance

Perhaps the most far-reaching assistance the Commerce Department provides to small- and medium-sized firms is our export promotion programs. With 127 commercial offices in 66 countries, and 48 district and 19 branch offices in the United States, the U.S. and Foreign Commercial Service (US&FCS) plays the leading role in assisting U.S. companies in the international marketplace. Many of these companies are small businesses which lack the resources to go it alone. Without our help, some would not be able to do business abroad.

Awareness Programs -- Our assistance begins with outreach programs. Our promotional techniques include direct-mail campaigns, targeted articles in industry publications, piggy-back advertising, and public service radio spots, many of them aimed at small businesses.

Currently, we are working with the Ad Council to develop an aggressive export awareness media campaign. Advertisements distributed to 3,500 major publications urge interested firms to call us on a toll-free telephone number, 1-800-343-4300 (Operator 199).

Getting Started -- Once firms are interested in exporting, we offer some basic instruction in how to go about it. Our newly revised Basic Guide to Exporting is a comprehensive "how-to" manual on the mechanics of exporting. Through our links with the 51 District Export Councils (DECs) and organizations such as local chambers of commerce, we will conduct over 3,400 export seminars this year.

Export Counseling -- Our counseling programs help small firms to pursue export leads without having to commit up front to additional staff and overhead costs. This year our district and overseas offices will conduct more than 100,000 counseling sessions with individual firms and government organizations. Our New-to-Europe program, is designed to take advantage of renewed opportunities for U.S. exports stemming from the dollar's decline and improved business confidence abroad. During FY1987, our objective is to help 1,000 firms make an initial marketing effort or introduce a new product in one or more Western European markets that they are not now serving.

Commercial Intelligence -- The best export counseling is custom-tailored to the needs of individual companies. Our trade specialists will soon have a new tool to enhance their capabilities in this area. The Commercial Information Management System (CIMS) is a computerized information system that will speed the flow of information on current overseas market opportunities to our offices and to the business community.

In addition, we have begun converting our market research information for on-line delivery. Right now, our district office trade specialists can access more than 5,500 market research abstracts using an electronic mail network.

We have also narrowed the focus of our research from broad industry reviews to sub-sector and product-specific studies, increasing its value to the small business community. A new service called Comparison Shopping can provide an interested exporter with concise answers to key questions about its product: overall marketability; names of competitors; comparative prices; customary entry, distribution and promotion practices; factors that may influence competitiveness; and information on trade barriers.

While this service is only available for 15 countries, the response of the business community has been enthusiastic -- 97 inquiries have been researched since the program began less than a year ago. One small business making electrodes for the medical diagnostic field established a distributor representation in England with $500,000 in sales in the first year.

Trade Promotion Events -- Finally, we offer U.S. business a varied menu of trade promotion events to showcase their products to overseas sales prospects: trade fairs, trade and seminar missions, catalog/video catalog shows, and business information offices. Last year, over 2,700 firms participated in ITA trade events. Fully half of them were small businesses, 30 percent were medium-sized firms, and only 20 percent were large companies.

A key strategy to increase participation by smaller firms is to increase the value of these events while keeping costs reasonable. A good example is our Matchmaker Program -- special delegations of U.S. businesspersons planned, organized and led by US&FCS officers. Our recent Matchmaker '86 in London gave 37 small- and medium-sized high tech electronic equipment companies the opportunity to meet 500 British business representatives. Early returns show that 21 representation/agency agreements were signed, 8 licensing agreements were negotiated, 10 joint venture partners were identified, $700,000 in equipment was sold off-the-floor, and potential 12-months' sales of $6 million are expected.

To reach firms that are reluctant to participate in overseas trade shows, we reinstituted an improved Foreign Buyer Program (FBP) last year. This program brings together American firms and qualified foreign buyers at U.S. trade shows.

To make the most of our resources, we seek out partners in our promotion activities. Through cooperative efforts with the Small Business Administration (SBA), we are better addressing the specific needs of the small business community. Many Small Business Development Centers now serve as associate offices of ITA. Currently, we are negotiating a memorandum of understanding with the SBA to further improve these linkages. Through the National Association of State Development Agencies, we are involved in a wide variety of cooperative ventures on the state level. And we have entered into an agreement with the U.S. Information Agency (USIA) to promote our foreign buyer program events during 1987 through Worldnet broadcasts.

CONCLUSION

In discussing the special situations and needs of small business we should not somehow assume that they can be entirely segregated from larger enterprises, or that they are in some way more or less virtuous or meritorious than their larger competitors.

America needs all parts of its economic machine to operate at full throttle, for each part depends on all the others for its success. A small spark plug is useless if it has no fuel to ignite or a large engine to drive. Nor can the large engine produce without the stimulus of the spark plug.

But smaller companies do have special needs. It is the responsibility of government to understand those needs, and to work for a business climate in which aggressive and innovative small businesses can successfully play their vital role in our nation's present and future economic success.

Thank you, Mr. Chairman.

PREPARED STATEMENT OF FRANK S. SWAIN, CHIEF COUNSEL FOR ADVOCACY, U.S. SMALL BUSINESS ADMINISTRATION

Mr. Chairman, I appreciate the opportunity to participate in your review of trade and competitiveness issues. Small businesses have an important stake in the outcome of Congressional action in this area. Perhaps more importantly, our national ability to increase our international economic competitiveness depends on continued growth of the small business sector. Policies that expand small business opportunity build on the strength of our economy; policies that protect us from change are policies that hurt small business.

Most small firms are affected by international competition. Whether or not you export or import, the product you produce or sell may be, and probably is, manufactured and available from a foreign source. Even if what you produce is not subject to trade competition, chances are that your customers or others with whom you do business may be subject to international markets. It is important to recognize that the ability to meet changing markets, to be competitive, is important to every business, not just these involved in international trade. The flexibility of our economy in all of its many constituent parts is essential to the competitive ability of those firms facing international competitors face-to-face. As a result, competitiveness policy must address not only import and export issues but also impediments to competitiveness that we impose on ourselves.

Surely we need to negotiate reduced foreign barriers to exports and we need to improve our assistance to exporters. But our long term success depends in considerable degree on our ability to tackle those regulatory and legal burdens which are, in effect, domestic barriers to competitiveness. Among the restrictive polices are the current hodge-podge of product liability laws, many proposed mandated employee benefits and regulation of the trucking industry. There are many others.

Much of the concern for competitiveness has focussed on the manufacturing sector. American industry is changing. Changes in technology, in distribution and marketing, in worker and consumer preferences, and in the speed with which information can be manipulated are all opening up thousands of new opportunities and forcing change on existing institutions. It is no longer true that bigger factories are necessarily better factories.

Evidence of the change overtaking American industry is abundant. The much publicized "bad news" of large plants closing or scaling back has obscured some important growth in small, lean, competitive small businesses. Without belittling the very significant personal dislocation that occurs as large manufacturers relocate or scale down their operations, the U.S. economy has in fact gained manufacturing jobs. Between 1976 and 1984, the U.S. economy gained about 1 million manufacturing jobs. While important, this 5.1 percent growth in manufacturing jobs is not as dramatic as the 14 million new service jobs added during that same time period. The raw numbers obscure other important changes. For example, one of the fastest growing service sectors is business services: personnel, word processing, accounting, payroll administration and consulting. Jobs in this area are occurring as manufacturers and other businesses contract out parts of their overhead functions, focussing their management abilities on their primary activity and leaving many tasks previously performed by staff to contracted firms. This increases the flexibility of the primary firm to respond to surges and slumps in its market. It also means that the modest growth in "manufacturing" jobs actually understates the job growth associated with manufacturing. Many of the new service sector jobs are jobs that, had they been kept in-house, would show up as manufacturing jobs since they would have been reported by a manufacturing firm.

The other trend obscured by the overall growth figures is the sharp contrast between small and large manufacturers. Between 1976 and 1984 small manufacturers created 1.2 million new jobs, offsetting the 130,000 jobs lost in large manufacturing firms. In other words, all of the 5.1 percent growth in manufacturing employment came from small business. As you know, manufacturing employment is not growing at an even pace everywhere. In metropolitan areas, large business manufacturers lost 207,000 jobs between 1976 and 1984, compared with small business growth of a little over 1 million jobs. In non-metropolitan areas, both small and large manufacturers grew, small by 185,000 jobs, large by 76,000 jobs.

This small business manufacturing growth occurs across the spectrum of manufacturing industries. Small business is growing in these industries, and prospering in the face of competition from large domestic firms and from international competitors. Small firms do this through their ability to be flexible and adapt to new technologies, the same qualities that make small firms succeed in domestic markets.

The small business record in manufacturing speaks for itself. In office and computing machinery production, small business employment (in firms with under 100 employees) grew 297 percent between 1976 and 1984. Small business employment in electronic components was up 115 percent, measurement and control instrumentation grew 136 percent and medical instruments grew 77 percent.

The role of small business is illustrated particularly in several areas where small business growth offset, to a degree, losses in large business manufacturing jobs. In the basic steel industry, while overall employment fell by one-third between 1976 and 1984, small steel manufacturers grew by 39 percent. The small, specialized mills that are growing are taking advantage of new technology; they may have lower labor, energy and material costs and are geographically dispersed, located near either sources of supply or their customers.

In the drug industry the small firm share of jobs has shifted as well, increasing from 10 percent of employment in 1976 to 17 percent in 1984. Changes in the regulatory environment, opening of the generic and over-the-counter drug markets has allowed new firms to grow. While total employment in the industry fell by 16,000, small firms added 18,000 jobs between 1976 and 1984.

These examples point up the danger of over-broad generalizations about the competitiveness of U.S. industry. As the U.S. economy changes, growth is occurring in many industries. While that growth is sometimes overwhelmed by declines in other parts of an industry, the overall growth of jobs in the economy reflects changing use of technology, changing consumer preferences and shifts in the comparative advantage of U.S. firms.

As a major part of the "economic adjustment" mechanism in the U.S. economy, small firms discover new markets, create new products, find new markets for old products and find new ways to accomplish old tasks. While not every small firm embodies all of these attributes, the efforts of thousands of small firms produce the result. The opportunity to try, and to succeed or fail, is a vital national resource.

What policies should Congress address to insure that small firms increase their contribution to the flexibility of the U.S. economy? I have earlier suggested three areas of focus: foreign barriers to competition, export promotion and domestic barriers to competition.

Small business owners with whom I have met over the course of 57 state meetings of the White House Conference on Small Business were overwhelmingly in favor of open and free international competition and opposed to protectionist legislation. Small firms succeed in domestic markets by competing in offering a better product or service at less cost. Small firms have no guarantee of business success This uncertainty sharpens their innovative abilities and makes them keen competitors. This view of how to succeed extends to their view of the international marketplace. Consequently, the success of the General Agreement on Trade and tariffs (GATT) negotiations in opening markets is important to small business. Similarly the expansion of the GATT to include services is important to small business. The growth and long-term strength of the U.S. service economy depends on our ability to obtain access to international competition.

Of immediate interest, the U.S.- Canadian free trade area talks are important in themselves and, as well, provide a rehearsal for many of the issues to be faced in Geneva at GATT talks. We in the Office of Advocacy are working with the Special Trade Representative's office to ensure that small business views are considered and heard in the U.S.- Canadian efforts. With specific interest in investigating trade issues in the accounting and advertising sector. Next week we will be meeting with small business owners in Buffalo, N.Y. and later in Detroit, Michigan to discuss trade problems they may be experiencing in these two fields. It is our hope that the effort to consult with small firms will prove sufficiently informative to be extended to the full GATT negotiation.

Export promotion is the responsibility of several Federal agencies, including SBA. The panel which follows can address our efforts at SBA in detail. Let me simply say that rather than new programs or more money, the single wish that I hear most from small business is for better coordination between Federal agencies and between Federal, state, local and private sources of export assistance. The White House Conference recommendation calling for a single trade department stems principally from this concern. The many steps underway at the Department of Commerce, at SBA and at the Export Import Bank make a major re-organization unnecessary in my view; but the call for better coordination cannot be ignored. Cross training of staff, joint provision of services, improved communications and increased attention to small business all should be on the current agenda.

In this regard I should note that we are focussing a portion of our Advocacy research budget on two issues that have emerged from the White House Conference on small business. Following a review process that is underway this month, we will award two research contracts: one to develop improved small business trade data and a second to explicate the "Export SBIR concept. The work on these contracts will take several months, but will be useful to the ongoing efforts to increase small business exports.

Eliminating domestic barriers to competitiveness is the main objective of the Office of Advocacy. Over-burdensome regulation, laws that foreclose opportunities and Federal mandates that sap small firms of their vigor are the targets of our efforts on behalf of small firms seeking to grow and prosper in the domestic economy. These same targets are appropriate to increasing the international competitive ability of U.S. firms and the economy as a whole. Delegates to the White House Conference on Small Business identified and called for action on many of these domestic barriers: tort laws, mandated benefits, the Federal deficit, the Davis-Bacon Act and 56 others.

The President's competitiveness package recognizes the danger of these barriers and proposes action in several important areas of small business concern. I recognize that it may be more tempting to legislate against foreign competitors than to take action on several difficult domestic issues that cost small business significant competitive advantage. I hope this is not the case. Whether the goal is increased utility for U.S. patents and copyrights, a freely functioning and flexible labor market, more rational allocation of risks of injury, or reduced domestic freight costs action to insure our long term competitive role in a world economy should begin with domestic issues. The Vice President is re-convening the executive branch review group to examine regulatory burdens. I look forward to continuing to work with Congress and with other agencies to insure that our policies do not limit our competitive ability. After all, these are burdens we place on ourselves without a foreign government or firm even lifting a finger to lessen the U.S. share of international markets.

Today total exports and imports represent twenty percent of our Gross National Product: by the year 2000 this will increase to more than thirty percent. The message is a simple one: we live in an increasingly international economy. Rather than hide from that change or seek to forestall it, we need to embrace the opportunity to change and to grow. I believe that our national ability to do that lies largely in the small business sector. As we have seen in many sectors of the manufacturing industry and in services, small firms are growing, finding new ways to accomplish old tasks, and discovering new ways to compete.

To promote this contribution by small firms there are three steps to be taken:

1. Congress should refrain from erecting inflexible barriers to change-forcing competition from international markets.

2. We must improve coordination of our export assistance efforts, working as well with state, local and private resources.

3. We need to reduce restrictions that we place on our own small businesses. This means chipping back regulations and laws that make it hard to innovate, to hire and train workers, or to provide products and services to willing buyers.

Mr. Chairman I look forward to answering any questions the committee may have at this time.

TRADE AND COMPETITIVENESS ISSUES

TUESDAY MARCH 24, 1987

House of Representatives,
Committee on Small Business,
Washington, DC.

The committee met, pursuant to notice, at 10:45 a.m., in room 2359-A, Rayburn House Office Building, Hon. John J. LaFalce (chairman of the committee) presiding.

Present: Chairman LaFalce; Representatives Mazzoli, Olin, Hayes, Flake, Lancaster, Campbell, Price, Slaughter, Gallo, and Hefley.

Chairman LaFalce. The Small Business Committee will come to order.

Today, our committee continues its series of hearings on trade and competitiveness issues. Through the hearings we have held thus far, our committee has identified some serious problems that face the small business sector of our economy in its efforts to compete both at home and abroad. Next week, this committee will be considering legislation designed to alleviate some of those problems.

The small business sector is often referred to metaphorically as the invisible hand that helps drive our economy. In the increasingly competitive international environment we face, that metaphor could become a reality. Smaller manufacturing firms are disappearing as U.S. multinationals rely increasingly on a foreign subcontractor base. Difficulties in acquiring and applying new technologies inhibit growth and revitalization. Capital formation is inadequate.

For too long, U.S. firms have been lulled into a sense of complacency because of the size of our domestic market. Increased foreign competition and the resulting influx of imports may well mean our domestic market may no longer be sufficient. We face a newly interdependent global economy, characterized by rapid changes in technology. In this new environment, increasingly sophisticated production and marketing strategies are required to compete—whether in Buffalo or in Tokyo. We must increase the ability of smaller U.S. firms, which have little experience and more risk to absorb, to export and to compete against foreign competition in our domestic market.

Public policy at the Federal level has done little to help. The Commerce Department laments the fact that 20,000 to 30,000 smaller U.S. firms have unrealized potential as exporters, while those firms which do try to export face bewildering bureaucracies and byzantine regulations.

The Export-Import Bank has numerous export financing programs designed to meet the particular needs of smaller firms. Yet, many of these firms do not even know the programs exist, let alone how to access them.

Our export licensing system creates insuperable obstacles for small high-technology firms with innovative products that have clear export potential. Minimal effort has been made to capitalize on the potential inherent in the export trading company initiative. Small manufacturing firms facing a heavy influx of imports have few resources available to them to make the changes in production and marketing strategies necessary to meet the competition.

If we are to have the export-led growth necessary to turn our trade deficit around, these things must change. It is time for the Federal Government to take seriously its obligation to create a public policy environment that will enhance the competitive prospects and opportunities of its small business sector.

In today's hearing, we will explore the competitive problems facing smaller manufacturing and service firms and examine how Government policy can best enhance their competitive potential.

This morning, we are pleased to have with us Mr. Lionel Olmer, former Under Secretary for International Trade, U.S. Department of Commerce; Mr. Edward Donley, chairman of the board, the United States Chamber of Commerce; Mr. John C. Rennie, president of Pacer Systems, Inc., and a member of the National Commission on Jobs and Small Business, representing the National Federation of Independent Business; Michael Campbell, president, NOVA Technology Corp., representing National Small Business United; Virginia Littlejohn, executive director, Professional Services Council, representing the Small Business Legislative Council; and Richard Barovick, executive director of the National Federation of Export Associations.

Before we hear from our witnesses, however, I would like to place in the record a statement submitted by Hon. Nicholas Mavroules who, regrettably, cannot be with us this morning.

[Mr. Mavroules' prepared statement may be found in the appendix.]

Chairman LaFalce. Do any members of the panel have any statements they would like to make before we begin?

Mr. Campbell. No statement, Mr. Chairman.

Chairman LaFalce. About 15 minutes ago, I got off a plane from a meeting of the Inter-American Development Bank in Miami. We discussed, primarily, Third World debt problems while I was there because I have been actively involved in that issue, as some of you know.

But in my conversations with the Finance Ministers of a good many of the countries, including Central Brazil, Mexico, Ecuador, Costa Rica, and so forth, a number of things stood out, but one thing in particular that stood out is a short while ago in Costa Rica, for example, everything they import, maybe about one-third of it comes from the United States, about one-third from Europe, and one-third from Central America, with a little bit left over for everybody else. Now they are importing more from Japan than they are from America. I just found that a very interesting commentary. Also, if our small business community might be able to access any market, it might be that potential market closest to us geographically.

With that, let us call on our witnesses in the order that I introduced them.

We will put the entire text of your statements in the record, and we would ask you to summarize your statements, if you could summarize them in a shorter period of time than it would take you to read them.

Historically, that has not always been the case, and if you feel that you might not be able to do that, then I would ask you to read them.

Mr. Olmer, would you please read your statement?

TESTIMONY OF LIONEL H. OLMER, OF PAUL, WEISS, RIFKIND, WHARTON & GARRISON, AND FORMER UNDER SECRETARY FOR INTERNATIONAL TRADE, U.S. DEPARTMENT OF COMMERCE

Mr. OLMER. Mr. Chairman, I think I can perhaps do a little better in terms of saving you time by leaving my speech aside, and for the record, and making just a couple of brief comments.

In preparing my remarks this morning, I reviewed a volume of speeches that I had made in the period 1981 to mid-1985 while Under Secretary, and it came clear to me that when I entered the Reagan administration in January 1981, it was with the belief that probably the greatest single contribution which might be made to America's competitiveness, and I used the term in 1981, was through increasing the involvement of small- and medium-sized businesses in international trade.

On reflection, in preparation for this morning, I have to come to the conclusion that it is one of my largest disappointments that that did not materialize. It is evident that the export trading companies are not being adequately utilized, the Eximbank is underutilized, the Export Administration Act is far more complex, not less, than we had hoped, and problems for small- and medium-sized businesses, because of the EAA, have multiplied geometrically.

Despite enormous efforts at promotion through hundreds of conferences across the country by the Commerce Department principally, there simply has not yet been a surge on the small- and medium-sized business community in terms of interest in international trade.

So, I think your hearings are enormously important to examine why it has not happened, to learn whether it is possible to make it happen, and how.

I have only a few suggestions that are contained in the testimony that I prepared for the record. I would say that the size of the prepared testimony is proportional to the staffs available to produce it. A few years ago, you would have gotten about 20 pages from me; you now have less than 5, and, so, while I will not argue that it is revealed wisdom, I do think there are a couple of useful suggestions in it and foremost among them, and I stop at this point, is that I think it essential that a small business office be created in the Department of Commerce to support small- and medium-size businesses in winding their way through the complexities of the technology transfer regulations, particularly companies that do not have Washington offices and must deal by telephone. It is an expense that discourages even the best and the brightest among them, and I believe that the Congress has recognized this before, and I am afraid not much progress has been made toward its expressed intentions.

I would be prepared to answer questions on that and related areas when it comes time to.

Thank you.

[Mr. Olmer's prepared statement may be found in the appendix.]

Chairman LaFalce. Thank you very much.

Mr. Donley.

TESTIMONY OF EDWARD DONLEY, CHAIRMAN OF THE BOARD, U.S. CHAMBER OF COMMERCE

Mr. Donley. Mr. Chairman, I have submitted a detailed report for the record, and, therefore, I will just make a very brief summary of the comments which I have before me.

First of all, I would like to establish my credentials. I do have a small business background. I am retired in December 1986 as chairman of Air Products and Chemicals, Inc., in Allentown, PA. I began to work for that company in 1943, when it had 10 employees. Today, we are the 237th largest industrial corporation in the United States with 18,000 employees, with operations in 18 countries around the world from which we export to 57 other countries.

I believe that I was fortunate in having a 40-odd year career in which the company was able to go from a very small entrepreneurial startup enterprise into a major international corporation, and I believe we are a very good example of what the contribution that small business can make to prosperity and jobs in the United States.

Now, for the future, what is needed? I will quickly summarize. We, in the Chamber of Commerce, believe that we need to develop and support policies and programs to increase exports; press for the elimination of foreign tariff and nontariff barriers to the United States trade and investment, and improve the ability of U.S. firms, particularly small business, to compete domestically by providing effective recourse to foreign unfair trade practices and injurious imports.

It is particularly important that attention be given to the small business community because I know from our own experience that when our company was very small and we did not have the staff and the resources to deal with these issues, it was very difficult to take advantage of foreign markets and to stem the tide of foreign products coming into the United States.

As we became larger, however, and had our own internal staffs, it was much easier to cope with the complexities of these issues.

So, I believe, Mr. Chairman, that your committee's attention to the small business sector and to its ability to compete in world markets is an extremely important way of contributing to the prosperity in the United States.

Now, some of the issues that we believe are most important:

First, strengthen the market access provisions in the agreements;

Second, approve new trade agreement negotiating authority;

Third, clarify the Foreign Corrupt Practices Act—this is very important to small business. I know of small companies who simply stay away from even attempting to export their products from this country because of the complexity of the Foreign Corrupt Practices Act. It is beyond the capacity of their limited legal staffs to cope with.

Fourth, provide improved procedures for the Export-Import Bank. We believe that private sector banking must play a role in the financing that the Export-Import Bank does not reach, and this aspect of the problem needs attention.

Fifth, strengthen intellectual property rights protection;

Sixth, mandatory retaliation, we believe, against foreign unfair trade practices would be in the interests of the United States, and I underscore the word mandatory. Discretionary retaliation merely provides a hunting license for foreign companies to come in to the United States with unfair and, in some cases, illegal practices.

In the Chamber of Commerce, we believe strongly in the President's competitiveness initiatives. We believe it is a comprehensive and reasonable approach to assure American competitive preeminence into the 21st century.

The summary of our statement regarding the competitiveness issue is attached to my overall statement, which we are submitting for the record.

I thank you, Mr. Chairman, for this opportunity to comment, and I would be pleased to answer questions if you have any.

[Mr. Donley's prepared statement, with attachment, may be found in the appendix.]

Chairman LaFalce. Thank you very much, Mr. Donley.

Our next witness representing, I believe, the National Federation of Independent Business, Mr. John Rennie, president of Pacer Systems.

TESTIMONY OF JOHN C. RENNIE, PRESIDENT AND CHIEF EXECUTIVE OFFICER, PACER SYSTEMS, INC., REPRESENTING THE NATIONAL FEDERATION OF INDEPENDENT BUSINESS

Mr. Rennie. Yes; thank you, Mr. Chairman.

My name is Jack Rennie. I am the president and chief executive officer of Pacer Systems, an aerospace defense contractor with headquarters located outside Boston.

I am accompanied today by Ms. Mary Jane Norville, assistant director of Federal Governmental Relations for the National Federation of Independent Business.

I am very pleased to have the opportunity to testify today on this matter because I think it is one that is certainly one of the most important topics regarding America's future and the future prosperity of America's small business sector.

I am here today in two capacities. First, I have submitted a statement on behalf of the 500,000 members of the National Federation of Independent Business, a broad ranging statement reflecting NFIB's thoughts and observations on the subjects of trade reform and international competitiveness within the small business sector.

I will also testify on my own behalf as one who has been involved in trade in my own company and as an activist nationally in the promotion of small business exporting for over 10 years. I am a former chairman of the International Trade Committee of the Smaller Business Association of New England [SBANE]. I was the first small business representative on the Industry Sector Advisory Committee on Aerospace [ISAC–1] under the Secretary of Commerce, and I have testified numerous times on behalf of small business organizations over the years on trade-related subjects before a number of Senate and House committees.

I am also the author-editor, on behalf of the Small Business Foundation of America, of a unique international trade source book for small business CEO's, called "Exportise", now going into its second edition.

Most recently, I had the privilege of being a member of the National Commission on Jobs and Small Business, which you, Mr. Chairman, and several other members of the committee convened in 1985. This commission gradually was drawn, through 15 months of hearings, meetings, and studies, to the international competitiveness theme. Hence, the title of its report, "Making America Work Again."

One section of that report with which I had a lot to do was the recommendation entitled, "Restore the Yankee Trader Tradition," summarized in the text at a very top level as follows:

> We recommend continuing the policy of the United States that supports fair trade of goods and services among countries combined with an aggressive, visible high-priority program to restore a vigorous exporting industrial base that will include large numbers of smaller firms.

Mr. Chairman, I do not want to take the committee's time at this juncture to reiterate all aspects of the items mentioned in the report, but let me for the record list the major topics which also reflect many of NFIB's points.

Expand the GATT to continue to emphasize services, intellectual property rights, and agriculture with emphasis on what I would call enlightened reciprocity within a general desire for freer and fairer trade worldwide.

Reexamination of import quotas so that unnecessary or unsupportable quotas can be eliminated and those in place that are valid can be enforced.

Providing incentives to attract new companies into U.S. exporting and to stimulate exporting companies to expand their efforts.

Improve the education of small business owners and managers so they can better understand the exporting process and the many nuances of trade abroad.

Improve the flow of marketing data so that U.S. companies will have a more timely and accurate understanding of the needs of overseas buyers.

Stimulate State action to increase trade, realizing that each State and region has different characteristics, and strengths, and in many ways they can most efficiently serve their local constituencies.

And, finally, convene an international summit of small businesses to develop better understanding of the ways of international trade from networks between small businesses and raise the visibility of small business and trade discussions.

As you know, Mr. Chairman, these topics were further broken down into more specific suggestions. All in all, I feel that this section of the report summarizes my feelings on the subject of what should be done to increase the small business sector's participation in exporting.

But I would like to take a few minutes to underline some very vital themes which I feel are not often fully appreciated when considering the subject. These themes are drawn from my time as an activist.

First, we should remember always that the underlying problem with trade in this country is that it does not have a high priority. Laws are passed, debates take place, people mouth words which give every appearance that we care, but in the end we have not, at least up till now. We are the only major industrialized Nation without an equivalent of a ministry or Department of International Trade.

We pass, potentially, very useful laws, such as the Small Business Trade Expansion Act, the Export Trading Companies Act, et cetera, but then we let the great public and private bureaucracies take over and smother or redirect the thrust of their implementations. We allow the mechanics of trade to bog down those who would take an interest: Over-complicated paper work, overly protective technology transfer restrictions, overly zealous laws to regulate trade practices or force U.S. ethics on other countries.

So, in short, whatever is proposed here today or this year or in this Congress will mean very little if we, the people, the Congress, and the administration, do not take trade and make it the second highest priority behind defense in the land.

Serve notice that we are coming to the international markets with a vengeance. I am fully convinced we must do this or we will just spend a lot of time and effort spinning our wheels, being beaten badly by our trading partners with the whole economy suffering as a result.

Second, in considering ways to improve our exporting, we must keep in mind that it is a long-term process. It is a penchant of America that we are short-term oriented, and it is hurting us badly. This is true for our short focus financial yardsticks, judging company and management performance on quarterly results; and it is also true in trade.

We rejoice, with some justification, if our month-to-month trade balance shifts favorably or a larger American firm lands a big overseas order; but the solution to our trade deficits in the long run will be found not in quick hit solutions, but on the slower, methodical and less glamorous effort to energize our smaller- and medium-sized companies into international markets.

Third, we must understand that we are unique in the world in that our large domestic market acts as a disincentive to go offshore, except for large companies, which have achieved a more or less stable domestic market share and the few companies geared to foreign markets from the outset in their formations.

This is coupled with an almost benign acceptance and openness to would-be competitors from overseas. Therefore, we must understand that it is in this country's best interests to energize America's smaller- and medium-sized companies to join the international fray, as it were.

Sure, it will benefit companies of all sizes, but just as surely as the company aids the U.S. economy when it succeeds, and grows and creates jobs, it is equally beneficial when that company begins to make its mark abroad.

So, where does this leave us? What can we do? Well, Mr. Chairman, you have received numerous good suggestions at these hearings, and I am sure your staff has uncovered others in its research, but I would start by saying that it is my impression that, in fact, a lot has been done. It is just that we are not making the most of what we have, and that is where I feel SBA and the context of these hearings can make a big difference.

There are all kinds of facilities, data, programs, and trained personnel available at State and Federal levels of government and in the private sector which could help. They are in place to help the would-be Yankee traders, but the small business community does not know where they are or how to use them.

Now, again, often you will hear the feeling, stated in different ways, that the resources are there, all you have to do is come in and use it. While this is a very human reaction, it is dead wrong. What we should say is that if the smaller- and medium-size firms are not using it, it is useless.

Certainly, the IBM's of this world do not need it. No; the only justification for these resources is to be used effectively by the smaller business community. So, I would recommend that the committee focus its attention on using available SBA resources to maximize the connection between in-place resources and the small business community.

Some examples that I can put forward are: First, use the network of small business development centers [SBDC] and other SBA facilities to actively market Department of Commerce programs, Eximbank facilities, et cetera, concerning trade, and feed back to these organizations, ways that the programs could be improved as they learn from using and working with small businesses.

Second, use SBA regional and district offices to seek out market data from the United States and Foreign Commercial Service and disseminate that information to small businesses in their area.

Third, SBA offices and trade specialists working with SBDC's should catalyse the formation of joint ventures with capabilities overseas.

And, finally, SBA should publicize the existence of and aid in small business using the facilities of the trade adjustment assistance offices located around the country to help those firms negatively impacted by imports in their markets.

In other words, SBA and its resources should become an activist in getting the small business community interested in participating in these markets and aware of what help there is available to overcome some of the mechanics and complexities of trade. This would be a highly visible and positive role for SBA, one that it could point annually to with pride.

Finally, Mr. Chairman, I would like to offer what I think is a specific novel idea, one which I hope the committee feels is constructive. As some members of the committee know, I have been involved deeply in Federal procurement matters with regard to small business as well, and it is intriguing to me that there are many parallels between selling to the Government and selling overseas, when taken from the small business CEO viewpoint.

I embarked on an effort, 4 or 5 years ago, to research the possibilities of the formation of a flow-through or go-between company that could interpose itself between the Government and the small business community to facilitate participation of small firms in Government procurement.

Almost right away, the lawyers determined that such a company would violate the Walsh-Healy Act. However, further research found that a long-overlooked provision in the Small Business Act, 15 USC 638(d)(3), authorizes the SBA Administrator working with the Federal Trade Commission [FTC] and the Justice Department to encourage the formation of what are referred to as small business defense production and research and development pools.

These pools, if properly formed, obtain important exemptions from antitrust laws, the Walsh-Healy Act, and from rules of affiliation as described in the SBA regulations. In short, there is an exemption which allows the formation of joint ventures between unaffiliated small companies.

Having found this forgotten feature of the law, I proceeded to put together the first pool of this kind ever formed as far as I know. It was comprised of six New England high-technology companies and was formally approved by the SBA, the FTC, and the Justice Department in 1984.

There were two aspects of these pools, once approved, that was intriguing to me. Although the members of the pool had to be small companies, the pool, once formed, had unlimited subcontracting capability, including companies not in the pool, small or large.

Second, although the primary purpose of the pool was to facilitate Government purchases to small business, there were no limitations on where the pool may market its capabilities, including international markets.

So, now, in the context of today's hearing, Mr. Chairman, I would propose that the committee, working with the Administrator, dust off this provision and seek to do two things.

First, expand the applicability of this exemption in the Small Business Act by amending the wording to include all kinds of manufacturing and services, rather than just defense production and the broader R&D category.

Second, if the applicability is broadened, update SBA literature, disseminate the information broadly through the SBA-SBDC network and begin to actively encourage and facilitate the formation of small business pools.

One can easily see that these pools can take on the form, very quickly, of a small business export trading company, and if properly staffed could provide a neat mechanism by which more companies would get into trade. The new pools [ETC] could act initially as an export management company [EMC] and then gradually take on the added features of an ETC as the pool resources grow.

The pool provisions, by the way, are very broad in terms of the form of the pool itself, from a loose consortium of companies to a formally incorporated company. Also, pools can be for profit or not for profit.

I feel there is a kernel of important wisdom in the small business pooling idea which essentially grew out of World War II. It just needs to be broadened and marketed to the small business community. I have extensive information on these pools should the committee need it, and I would be happy, of course, to provide this to the committee staff.

In conclusion, Mr. Chairman, let me personally and on behalf of NFIB congratulate you and the committee for your interest and perseverance in this vital area of trade reform and international competitiveness. Our problems in getting the small business sector into trade are unique in the world. To succeed, we must go to unusual lengths to make it happen. But if we do, the country and the small business community will be better off, and I believe SBA will have found one area of activity where it can make a special contribution, a very positive contribution to America.

Thank you, sir. I would be happy to answer questions.

[Mr. Rennie's prepared statement may be found in the appendix.]

Chairman LaFalce. Thank you, Mr. Rennie.

As a point of information, I introduced the Carter administration's Export Trading Company bill, and then I introduced the Reagan administration's Export Trading Company bill, and we were able to get that enacted as a law in 1982. It has not done the job. As a matter of fact, the Banking Committee is having a hearing on that this afternoon, and we are going to be making some changes in that. I have coauthored those along with the chairman of the Banking Committee.

But I have also told my staff to explore ways to create small business trade companies, small business management companies, and you obviously have pinpointed a provision of existing law under which that possibility already exists and might easily or not so easily be expanded upon. It is something we will be working with you on.

Thank you.

Our next witness will be the representative of the Small Business Association of New England and also the National Small Business United, Mr. Michael Campbell.

TESTIMONY OF MICHAEL CAMPBELL, PRESIDENT, NOVA TECHNOLOGY CORP., AND CHAIRMAN, SMALLER BUSINESS ASSOCIATION OF NEW ENGLAND, INC., REPRESENTING NATIONAL SMALL BUSINESS UNITED

Mr. Michael Campbell. Thank you, Mr. Chairman.

Thank you for the opportunity to testify here today on behalf of National Small Business United and our representation of 12 regional associations, 15,000 individual companies, and 42,000 overall membership.

I will keep my comments fairly limited to three areas that I think are of the greatest need in order to get the job done for the small business community.

Simply speaking, what we feel that is needed today are workable solutions that will really act as a direct catalyst to prime the pump and promote international trade in the form of export sales and create new jobs.

Really, what is not needed today is grandiose legislation that, once it is enacted, is difficult to understand, cumbersome to implement and, in the end, dies on the shelf for these same reasons.

Accordingly, as I see it, the bottom line to the problems we have in international trade really lies in three major areas. Education, incentives, and Government cooperation.

Education. With small business, there is a major need for trained, qualified staff at the administrative level to get the export paper work done correctly and get the shipments out the door.

This is defined in terms of more of a factotum, someone that is well-trained to handle and understand all parts of export legislation, and do it at an affordable price to the small company.

The major differences between big business and small business is the resources of personnel, and is almost always manifesting itself in the international department. Historically, within the United States, small businesses spend so much time dealing with the domestic market that the international market has taken short shrift. Evidence of this fact is the growth of our domestic consumer market which has risen from a population base of around 160 million, at the end of World War II, to 239 million today.

However, although the importance of international trade has been lost to some extent on U.S. small business, it has not been lost on our competitors overseas.

In order to get technically qualified international personnel, we recommend that you look at utilizing the SBDC's on a local basis, and also encourage the local community colleges to provide people who would be affordable, and would have some knowledge of international trade to get small business actively involved.

The second major problem we see is incentives. We can create wonderful solutions and new legislation to solve the problem, but unless there are the incentives to go along with it, to stimulate small business to do something about it, it is, again, not going to go very far.

To this end, create a financial incentive in the form of an export tax credit, which would work similar to the investment tax credit which was just recently passed out of the last tax legislation. Such a tax credit would enable several things to happen. It could be taken in terms of training; it could be taken in terms of working to retrain redundant personnel; people who lose or have lost their jobs due to import competition; and finally, form the basis of a financial encouragement for small business to set up international departments within their own organizations.

Finally, the last matter I shall address is Government cooperation. The major resource that small business has at this time is the Department of Commerce. It makes no sense to me when I hear that international trade problems are as large as what they are when Congress is talking about passing an $88 billion highway bill. Yet, when we talk to the International Trade Group of the local Department of Commerce in the Boston office, they do not even have brochures to give out to encourage people to trade overseas. I find this paradoxical, and, as a citizen, I am unable to understand the reasoning or the politics behind it.

For the small business person, the Department of Commerce is probably their best opening to overseas markets. As a rule, they are a very qualified group. They are likewise a very competent group both domestically and overseas. In the overseas offices, I have even put together a couple of deals myself just through the local knowledge of the individual trade representatives in the consulates in Switzerland, Germany, and England.

But it does not make much sense to be sitting here talking about promoting trade for small business if we are taking away the resources of the Department of Commerce to such an extent that they have nothing to be able to promote the United States small business trade on an overseas basis.

That is about all I have to say. The rest of my comments are in the testimony I have presented to the committee, and I will entertain any questions afterwards.

Thank you very much.

[Mr. Campbell's prepared statement may be found in the appendix.]

Chairman LaFalce. Thank you very much.

Our next witness will be Ms. Virginia Littlejohn, chairman of the Committee on Economic and Regulatory Issues of the Small Business Legislative Council.

TESTIMONY OF VIRGINIA LITTLEJOHN, CHAIRMAN, COMMITTEE ON ECONOMIC AND REGULATORY ISSUES, SMALL BUSINESS LEGISLATIVE COUNCIL

Ms. Littlejohn. Thank you, Mr. Chairman.

My name is Virginia Littlejohn, representing the Small Business Legislative Council.

We have 90 member associations representing the interests of more than 4 million small businesses.

International competitiveness should provide a clarion call to new purpose and resolve, a new challenge for us to rise to, just as America rose to the Sputnik challenge in 1957. But, in my opinion, the current challenge is even greater because what we face now has far more sweeping impact on lives than the national humiliation of Sputnik.

Foreign competitiveness gnaws at the fabric of American life, taking away jobs and reducing income, hurting families, increasing alcoholism, child and spouse abuse, depressing villages, cities, State and regional economies, and devastating entire economic sectors.

In addition to the specific issues that you raised in your letter of request for testimony today, Mr. Chairman, which I have addressed in my written remarks, there are several other issues of overwhelming importance to international competitiveness which I would like to address verbally because I believe that they provide a context for the rest of the debate to be meaningful.

First, and absolutely fundamental, is the inadequacy of America's economic data and statistics. Lack of sound data is a practical barrier to understanding the nature, dimensions and character of the new American economy and the trade arena in which all of this is taking place.

Management expert Peter Drucker has stated that:

> The aggregates on which all statistics are built are now 50 years old, and, so, the great economic aggregates have been reliable plus or minus 40 percent. If you get that much slippage and still base policy on it, your chances of doing the wrong things are simply too great.

A prime example of inadequate data and statistics is the professional and technical services sector.

Until January 1987, the standard industrial classification or SIC codes did not contain a rational classification system for professional services. Most were listed under services not elsewhere classified. With the 1987 SIC code revisions and new numbers assigned to subsets of the industry, preliminary research indicates that instead of the $35 to $50 or $70 billion a year that we had thought the industry consisted of, it is, in fact, a $165 billion-a-year industry.

To marginally revise our SIC codes at 15-year intervals is, in my opinion, a national disgrace in an era when entire industries are born and die over the course of a decade.

The impact of inadequate data and statistics can be even more profound when applied to such important public policy debates as the U.S. trade deficit. Preliminary data for 1986 show that last year's trade surplus in services averaged about $44 billion, helping us to offset the deficit in goods trade of almost $150 billion.

The Government of Canada recently reported that America's surplus trade in selected services with Canada was many billions of dollars higher than the United States had reported, essentially double what we had believed because of our wretched statistics. This is not surprising when one realizes that the United States has 10,000 categories to measure trade in goods and now with 70 percent of the American economy in services, to measure trade in services, we have 40 categories.

Congress' Office of Technology Assessment estimated in a report last year that as much as half of the Nation's exported services may escape official statistics, and if you can believe it, we do not have a category for measuring computer software which is clearly one of the most important service-related products in a high-technology economy.

Citing the difficulty of trying to come up with real numbers about trade, statistical expert David Birch of MIT commented, somewhat ironically and sarcastically, but with, I think, more than a grain of truth, several weeks ago, that perhaps our international trade in services data are so understated that we may not even have a trade deficit.

Until America gets serious about updating its statistical aggregates, we will never be able to realistically measure where we have been, where we are going, or know when we have gotten there. As baseball legend Casey Stengal said, admittedly in a slightly different context, if you do not know where you are going, you might end up some place else.

While this is officially outside of the jurisdiction of the SBA, I do think it is critical that this committee provide additional leadership on this issue with your colleagues and other committees because until we have a base line for knowing where we are going, I do not think we can really address trade very effectively.

Another important cornerstone for enhancing America's ability to compete globally is making a substantial investment in human capital through education, training and retraining. Bruce Merrifield, Assistant Secretary for Productivity Technology and Innovation at Commerce, puts the problem bluntly:

> Life-long reskilling of the work force will now become a critical problem because any set of skills may be obsolete in 5 to 10 years. The great frontier of American education is now going to start at 22, after we get out of school, and continue all of our lives.

There are many glaring deficiencies in the area of training, some detailed in my testimony. I will cite only a couple. There has been no sustained public policy toward training to support vocational schools, community colleges, and public service employment. The Federal Government has adopted and abandoned an astonishing 14 different training programs since 1962, and our supply of engineers and technical specialists is shrinking rapidly.

By the year 2000, we may have a shortage of 15 million scientists, engineers, skilled mechanics and semiskilled workers. Another key education issue, and this has been touched on by some of my fellow panelists, is our inability to understand the language and culture of countries that we are trying to compete with and export to, and this is compounded by the paucity of managers trained in global trading issues.

Effectively educating managers on foreign markets, language, and culture is essential if we are going to be able to step up our foreign trade. One superior mechanism already exists which, if expanded, could greatly enhance the ability of American business to understand foreign business practices.

For 40 years, the Fulbright Program has supported an exchange of American students and academic scholars with students and scholars from other nations. The time has come to expand the Fulbright exchanges to include individuals in businesses of all sizes, offering short-term exchanges of 3 to 6 months and full year exchanges along the lines of the traditional Fulbrights in both cases preceded by an intensive language and cultural training program.

I believe that the Small Business Administration could play a role in promoting such a program and encouraging small business leaders to become active in it. Exchanges such as these should not be limited to countries of Western Europe, but should also include Latin America, the Pacific Rim, and the Far East, Africa, and the Middle East.

I applaud very much your leadership, Mr. LaFalce, and members of the committee for calling for the creation of a national commission on jobs in small business. Countless superior recommendations, which SBLC endorses, emerged from the commission report related to regaining our Yankee trader tradition. Those are largely outlined in my testimony, and I will only mention a couple verbally.

Expanding the scope of the general agreement on tariffs and trade to include services, agriculture and intellectual property rights, as well as greater consideration of small and midsized businesses in GATT.

More aggressively disseminating information concerning programs of the International Trade Administration already available to smaller firms, working through existing business groups, and I would like to parenthetically mention that I have worked closely with both the Department of Commerce and the SBA on two service-related trade missions led by the National Association of Women Business Owners, of which I am past president.

One of these was to Europe and one to Japan, and without any question, the quality and amount of assistance that we got both from Commerce and SBA was absolutely A plus. We were working with the national offices in both cases, and as several of my other panelists mentioned this morning, the problem, really, is that the information is not available in the field.

Both of those entities worked with us in identifying the countries we should go after, the particular sectors that they thought had enormous export potential in those areas, helped us identify members of the organization who had the potential to move into international trade.

NAWBO has 2,700 members; when we started the first trade mission, it was about 2,000, and I believe that within the membership right now, we have at least 200 members who are interested in moving into trade, and we are working in a very, very close way with SBA and Commerce on education and training of our members. I personally think that with the right kind of management and technical assistance and the right kind of walking through the process, the right kind of promotion, that we would, in fact, find there are many more firms than the 22,000 that have been indicated in all previous reports who would be interested in it.

I would also like to say that NAWBO is affiliated with an international organization of women business owners. It is a 25-nation organization, called the World Association of Women Entrepreneurs. In that organization, the leadership meets at least three times a year—the presidents of the various countries, and we have one annual world congress every year where we have between 200 and 500 women entrepreneurs from around the world who are meeting. The next one of those world congresses is going to be hosted by NAWBO in Denver in June, and we have found simply remarkable business opportunities growing out of that international organization.

So, I would like to underscore the recommendation that Mr. Rennie made about the utility of an international small business summit conference, where there is also strong governmental representation.

The importance of promoting the programs that we have right now is absolutely critical. Also, we endorse creating incentives for multinational corporations to use U.S. small and midsized businesses as subcontractors in overseas projects and providing incentives for large companies to assist small and midsized firms abroad in use of facilities and market leads.

I believe that there is a very large number of resources already on hand. I have mentioned several of them. I would like to mention also, along with several of my colleagues, the Small Business Development Centers, which I think could heavily move into this area and do a great service.

One other area that has an important relationship with what I believe is the effective development of international trade is effectively utilizing Federal procurement. A $200 billion annual market for goods and services which is one of the most direct ways in which Government can stimulate innovation, productivity and competitiveness in the American economy.

To do so, steps must be taken to streamline and simplify procurement while at the same time opening up access to smaller firms and building incentives for firms to move into international markets where they have capability domestically that can be expanded internationally.

Unfortunately, it appears that, many times, policymakers do not understand the relationship between domestic policies and international competitiveness. While in one breath they state their ardent support for expansion of international trade in services, in the next breath they cripple that very sector through flawed procurement policies.

Recently, for example, the Federal Government disallowed the expenses for Federal contractors in professional and technical services for traveling to France for the Paris Air Show, the most sophisticated in the world, and a critically important marketing form for smaller firms trying to break into international trade in aerospace and related industries.

Similarly, the professional and technical services industry is currently taking body blows as the result of an interim rule on profit policy recently issued by DOD and sustaining the potential for 20- to 50-percent cuts in profits if these rules are not changed.

The professional and technical services sector, $165 billion a year, is at the cutting edge in such fields as software development, artificial intelligence, systems design and integration, test and evaluation, and many other sectors with probably a 5- to 10-year competitive lead over Japan and other industrialized countries in many sectors.

Federal policies should nurture and support this and similar dynamic new industries rather than erecting barriers that undercut them domestically and damage their potential for export.

One way to dramatically highlight some of the problems raised is with a congressional call for a commission to be funded by the private sector as was the National Commission on Small Business and Jobs. Such a commission would review the state of data and public policy with relationship to the new services information and technology driven economy with particular emphasis on technology-based industries and highly skilled sectors that enhance our competitiveness in the world economy.

To continue to dismiss America's service economy as one where people take in each other's laundry and serve each other Big Mac's demonstrates a profound lack of understanding of the new American economy and of the synergism between services and manufacturing, which I think the chairman understands from his congressional district.

In concluding my remarks, I would like to note that Washington's biggest buzz word in years, competitiveness, means markedly different things to different people. How we ultimately define this term will be a test of our vision, our leadership, and our national resolve.

Because of your leadership, Mr. Chairman, this committee for the first time provides a unique forum to help define the term, sharpen the debate and force the pace. Please go to it with a vengeance because our economic future, as Mr. Rennie indicated, very much depends on it.

Thank you.

[Ms. Littlejohn's prepared statement may be found in the appendix.]

Chairman LaFalce. Thank you very much, Ms. Littlejohn.

Our last witness will be Mr. Richard Barovick, the executive director of the National Federation of Export Associations.

TESTIMONY OF RICHARD BAROVICK, EXECUTIVE DIRECTOR, NATIONAL FEDERATION OF EXPORT ASSOCIATIONS

Mr. Barovick. Thank you, Mr. Chairman.

Our association is basically representing the export management company industry and it was set up in 1984 to provide a Washington voice for that industry. It was somewhat inactive last year, and has been revived this year and I was asked to become the executive director back in January.

The federation consists of NEXCO in New York, which is an association of export management companies that has been around for many years; the Export Managers Association of California, the same; the Overseas Sales Marketing Association in Chicago. Those are the core groups, and, joining us as an associate member, is the Overseas Automotive Club, which is based in New York and New Jersey, but has a great part of its membership in the Midwest and is nationwide in membership.

Between the four groups, we have a membership of about 500 export management companies. Export management companies sell the products of small manufacturers. If each of our members sells the products of 10 manufacturers, it means that we are representing 5,000 manufacturers. If each of those small producers exports through our group half a million dollars a year, it means we are accounting for $2½ billion in exports.

If we could encourage an expansion to $1 million per manufacturer, we would be representing $5 billion. A sizeable sum and worthy of attention by the Federal Government.

Now, I, personally, am a journalist and a consultant. I have been in Washington for 19 years. I publish a couple of newsletters, "International Trade and Investment Letter" and "Eximbank Letter." The latter covers trade finance, and I provide information services to business. Actually, most of it has been to large corporations and large exporters. So, I have welcomed this opportunity to come on board as an advocate of small business exports and particularly of the export management company industry.

I will make a couple of introductory remarks, if I may, and then get on to what I think are some of the problems. The export management company is the export representative or department of a manufacturer. In a sense, it is small business coming to the rescue of small business.

The export management companies are small. There are some that are literally 2 or 3 people in the shop, going up to 75 or 100 employees. They either get a commission for the exports that they have achieved or, as is increasingly the case, they buy and then sell the products themselves and arrange the financing.

In a few cases, export management companies actually represent overseas some very large U.S. corporations. For example, one of our members specializes in food products and food processing machinery. That company is very active in the Middle East and in the Asia-Pacific areas. It represents several very large U.S. corporations in those areas. Why? Because it is well entrenched, has a good network, a marketing network on the ground, and is able to work that niche on behalf of large companies as well as small.

Now, in recent years, just as large companies have been battered in the export market, so have our smaller export management companies. The items that are on the front page of the newspapers, the high value of the dollar until recently, the third world debt, which have made it very difficult for U.S. exports, have obviously affected our industry, and to an exaggerated extent, because we represent firms that are smaller and therefore have limited resources and limited ability to respond.

However, now, with the dollar down and U.S. product quality improved, our industry feels that it has a new crack at getting into exports in a bigger way.

Trade finance is a serious problem. As you probably know, there was a National Foreign Trade Council study on the subject. That is a New York group comprised primarily of major corporations and a few large banks. They did a study of the trade finance situation in the United States. I will give you a copy of their summary. They concluded that the commercial banking industry in the United States has largely withdrawn from export finance.

In my newsletter capacity, I have spent the last year interviewing about 75 banks across the country, and I have found the same experience. The U.S. Export-Import Bank has drawn the same conclusion, and it is a real problem for industry.

Let me make a couple of other points, general ones, and then make a few recommendations.

The first point, I think it is important for the small business community to try to focus its attention, its resources, which are limited, on practical steps and practical programs in Government that can help small business exports.

We, as an industry, have our own particular requirements which I will mention, but I think that, unfortunately, much of the dialogue in Washington on exporting is in the policy arena. We are worrying about things that are basically of a foreign policy or regulatory nature.

Exports in the United States go basically like this—80 percent of our exports are handled by about 200 major corporations. Another 10 percent is handled by the Japanese trading companies in the United States, and the third 10 percent is small business or small and midsized business, including our industry.

The dialogue has tended to be focused on issues that are of interest to all across the board. I think it would be helpful for small business to recognize that those foreign policy issues are going to be resolved or not resolved by the major exporters and try to concentrate its limited attention and resources on practical steps for small business.

Someone mentioned the problems of the Commerce Department budget. I would note one thing, which I, as a newsletter publisher, have experienced personally. The Commerce budget was cut about 40 percent last year and 10 percent of it was due to Gramm-Rudman, but the other 30 percent was due to the decline in the value of the dollar. As the dollar declined, in order for Commerce to deliver its product overseas, it had to spend more dollars because the dollar bought less.

As a result of that shift, Commerce cut in the domestic side of its operations in order to sustain its activity overseas. One of the things that it cut was its publications subscription budgets, so I am aware of it. It would interest you to know that the field offices, the district offices of the U.S. Department of Commerce—there are 48 or 49 across the United States—do not have a budget to subscribe to the local newspapers or to the Wall Street Journal. Imagine our Commerce Department offices not having those basic resources.

We as an industry have a particular recognition problem. We feel we are a solution or an alternative, an option, for small business exports. Some small companies can go it alone and export on their own, but others would benefit from exporting through an export management company. It is no secret what we do.

Now, we have the following recognition problems. I will give you symptoms of the problem that we have got.

There is no SIC number for trading companies. If we could get an SIC number, we would know what trading companies in the United States were doing and we would have some data. The Commerce Department is aware of this, but I do not know what is being done about it, if anything.

Each year, the Commerce Department publishes the "Industrial Outlook of the United States" for the year ahead. This year, in all credit to Commerce, for the first time, they had a separate chapter on trading companies. Now, that meant a kind of official recognition of the trading company field. It is a little bit, I suppose, like Moscow on May Day—either you are on the parade grounds or you are in Siberia. We finally are on the parade grounds and we have been recognized as an industry in that official book of the Commerce Department. That is a step forward.

Another experience that I had recently and I am sad to report this, is that in the Washington Post, I have got this in my testimony, the National Commission on Jobs and Small Business was interviewed in February. Mr. Beard was interviewed and his comments on small business exports were that it is very difficult for small business and he said there is no mechanism, either in the private sector or the public sector, combined, to stimulate that, meaning exports.

Well, here we are. We now have our letterhead printed and I will send Mr. Beard a letter saying that export management companies are certainly available and have been for a hundred years to take on the exports of small business.

The most significant neglect of small business exports or, let us say, of export management companies, was the 1982 passage of the Export Trading Company Act. I am reminded of a remark I heard many, many years ago by Carlos Romulo, who was at that time the minister of foreign relations or the secretary of foreign relations of the Philippines. He said, in 1519 or whatever, Magellan crossed the Pacific and discovered the Philippines, and there we were. And the same thing happened in 1982, Washington discovered export trading companies and, by God, there we were, but we were not recognized, and, so, the 1982 Export Trading Company Act was basically built on the conception that there was a gap in the United States—that there were no trading companies. We had to emulate the Japanese and, therefore, we had to stimulate and set up trading companies to take on the export efforts of smaller companies that would not be positioned to do it.

Well, the results of the 1982 Act have been mixed. There have been some good things and there have been some bad. Our industry naturally regarded it as an effort that failed to recognize our contribution at all. On the other hand, in the case of the banks, I have talked to every bank, et cetera, in the United States. There are 42 banks that have entered into export trading company activities. I can give you a summary of what the banks have done in the field.

Of the 42, about 21 have dropped out. They have dropped out partly because exporting is very difficult. At the period they got into it, they could not have gotten into exporting at a worse time, for the same reasons that have impacted our industry.

But, they have also done some helpful things. A few of them, only a few, have used their trading company affiliate as an export credit device, and I will mention three. Manufacturers Hanover in New York, the U.S. National Bank, I think it is called, in Portland, OR, and Union Bank in Los Angeles, take title to the goods and thereby close the gaps so that a small exporter is able to achieve the financing because the bank now owns the product and can bring its own financial resources to bear on the transaction.

Manufacturers Hanover is just starting a new program to utilize its export trading company for that purpose.

On the antitrust side, the other side of the Export Trading Company Act, we have benefited just by coincidence. A combination of the 1984 Shipping Act and the Export Trading Company Act, absolutely unrelated to one another, but the two in combination have made it possible for exporters to set up shippers associations and these associations can negotiate as a group with ocean shipping lines, and they can achieve more favorable freight rates and, so, the unit in New York, NEXCO, of our four—Association Federation, has set up a NEXCO shippers association and they are now negotiating favorable freight rates for exporters and, curiously, some large companies as well as small exporters are climbing on board the NEXCO shippers association.

Congressman Ireland, I know, is interested in one aspect of this that I would like to just mention. This year, either as part of the omnibus trade bill or as a separate bill revising the Export Trading Company Act, proposals are on the table to change the 1982 Export Trading Company Act. Part of the changes would address the antitrust side to make it a little clearer, but part of it addresses the bank trading companies.

I would like to bring this to your attention because it is a rather disheartening situation. The administration is proposing the following: In the definition of what is a bank export trading company, the 1982 law said that a bank export trading company must be primarily engaged in exporting, primarily. The Federal Reserve——

Chairman LaFalce. Principally.

Mr. Barovick. Principally, principally. Right.

Chairman LaFalce. And an adamant stance.

Mr. Barovick. Right. And the Federal Reserve interpreted that, set up some regulations and the regulations say that 51 percent of a bank trading company's activity must come from exporting. It can also import. It could do third country transactions in which there is no U.S. product being traded, but 51 percent must be generated by U.S. exports.

Now, the administration bill and Mr. Bonker's bill both propose that third country transactions be counted as exports. Now, what that means, it is true that the banks have had a little bit of difficulty because now the Fed counts the third country transactions as imports whereas it would probably be sensible not to count them at all and just deal with the U.S. trade flows.

But what the administration is proposing is that third country transactions be counted as exports. Now, just imagine what that means potentially. It means that the money center banks—only a few of them that are in this field, in the trading company field—the money center banks can do third country deals and count them as exports.

The door is thereby opened that they do no exports. None from the United States, simply arrange transactions abroad, and get that to count as export operations.

We have just a few recommendations, and I will go through them in 2 minutes. We would like to see Government, Commerce, SBA, and the State and local governments across the country engage in an awareness program to bring to the attention of small manufacturers of exportable products that EMC's, export management companies, are available.

Second, we would like to see some kind of networking facilities set up whereby Commerce, SBA, the State and Federal governments, as a matter of course and in a low budget way, just notify small business manufacturers that would like to export, that export management companies are available.

We, as a federation, can provide them with the names of our members. They can use their own business judgment in hiring somebody.

On the trade finance side, there are a couple of bright spots at the Export-Import Bank. The Exim has a new association policy which can be utilized to help small business exporters through an association. In addition, Congress changed the Eximbank law last year, so that——

Chairman LaFalce. Mr. Barovick, I am going to have to ask you to try to conclude your remarks within a couple of minutes.

Mr. Barovick. Well, OK.

Today, a small business exporter, an export trading company, can go to Eximbank, borrow funds and lend it itself to a foreign borrower. Until now, only a bank could go to Eximbank, borrow and then lend. Now, on a medium-term transaction, an exporter can go to Eximbank, borrow the money and then lend it. That could be useful to trading companies, including perhaps ourselves.

I will stop there. The rest of the recommendations that I would suggest are in my testimony.

Thank you.

[Mr. Barovick's prepared statement may be found in the appendix.]

Chairman LaFalce. Thank you very, very much.

This has surely been a very interesting hearing.

Before we go to other members of the panel for questions, let me just ask one basic question. Is there anything that any member of the panel said that another member of the panel feels strongly enough about that you would wish to either underscore or take issue with it?

Mr. Donley. I would like to make an offer in response to that, Mr. Chairman, that the U.S. Chamber in the White House Conference on Small Business was held, we offered our facilities, our meeting rooms, our staff, and so forth to facilitate those meetings, and we would make that same offer if a national conference on small business exports is held as was suggested by some of my fellow panelists.

Chairman LaFalce. All right. Thank you.

Mr. Rennie. Mr. Chairman, I could underscore one thing that was said by the last witness. In 1981, the Smaller Business Association of New England—it really ranged over 1981 and 1982—did a survey of its membership and, in particular, zeroed in on those members—which amounted to about 8 percent of the membership, about 150 companies at that time—who were actively involved in exporting.

Only 5 percent of those companies which were actively involved in exporting even knew of the existence of EMC's, the export management companies. This was just shocking.

Chairman LaFalce. They did not have a trade association that had a letterhead at that time.

Mr. Rennie. Well, we even have members, in fact. Mr. Campbell here ran an EMC, and I guess still does.

But, in any case, it underscored that there is a great lack of understanding and knowledge in the small businesses, even those involved in trade, as to what is available to help them out.

When I got encouraged to get into trade in 1977, probably the single biggest factor was that through a combined Massachusetts Port Authority and SBANE Program, they took a limited number of companies at a time, five or six at a time, and gave us a full day of briefing of who was around that could help us; freight forwarders, export management companies, and others, international parts of banks, none of which I had any understanding of whatsoever at the time, and I had been in business then for almost 10 years. And that was the great factor in my thinking of getting into trade because I felt if I got a reaction from the overseas buyers or potential buyers, I could assemble a team of people to help me or, short of that, using the EMC or some such organization.

So, it just points out that there are these facilities around and we just have to do better in my mind to get the word out to the small business community that they are not alone and they are not in trade at all or are in it up to their eyeballs. There are ways that they can get adjusted and get into trade while minimizing or at least limiting their risks.

Chairman LaFalce. Mr. Mazzoli.

Mr. Mazzoli. Thank you very much, Mr. Chairman.

Thank you, gentleman and lady.

Mr. Donley, do you still live in Allentown?

Mr. Donley. Yes.

Mr. Mazzoli. Do you? Next time you see Bishop Welsh, if you would give him my best wishes. He used to be our bishop in Arlington, and I remember he was recently transferred to Allentown. Is he feeling better?

Mr. Donley. He was very well 4 or 5 days ago,

Mr. Mazzoli. He had that accident not terribly long ago.

Mr. Donley, on page 5 of your statement, you talk about something that is very interesting to me because in a recent meeting of our chamber at home, this topic came up in two or three different forms. That is the fact that Congress—inadvertently, at least—made an error in the 1986 tax bill, which, as you know, did away with capital gains treatments, did away with investment tax credits, did away with the ACR.

You, and also my friend, Mr. Olmer—I will talk to him in just a second—suggest that there might be some changes which could be brought to pass. Now, there are a lot of political problems in going back into the 1986 tax bill, but our chairman, to his credit, is having these hearings with a very laudable goal of suggesting elements that could be fit into this new trade bill coming through with respect to small business.

So, may I ask you to address that and how you personally, and the chamber, see that, and then I could talk to Mr. Olmer, who also mentions that in his statement, and any of the other panelists?

Mr. Donley. Mr. Mazzoli, in the 1986 tax bill, after swallowing hard, we supported it in the U.S. Chamber of Commerce because we felt that the lower marginal rate would have a modest stimulative effect on the economy overall.

I must underscore that we swallowed very hard in doing that because, as you said, that tax bill was adverse to new capital investment. It is adverse because of the changed cost of capital. It is adverse to entrepreneurship because of the capital gains tax rate, and it is adverse to research and development because of the more severe treatment of research and development expenses.

It is also, compared to the tax policies of most of our trading partners in the world, adverse to export from the United States. They, as you know, are allowed to deduct what, in effect, is a consumption tax under GATT.

It is my view, as a businessman, that we in the United States will be required to revisit taxes and correct those flaws if we are serious about making U.S. industry competitive in world markets.

Mr. Mazzoli. Thank you.

Mr. Olmer, welcome back. I remember the years when you were Under Secretary, and I saluted your efforts then and I salute them in the private sector.

Would you address, somewhat, what Mr. Donley did and what you have in your testimony as well?

Mr. **Olmer**. I agree with what Mr. Donley said, and the remark in my testimony suggests that perhaps a sliding scale of permissible deductions could be structured that would decline as the size of business increased.

In other words, that the allowances for R&D, the accelerated cost recovery, could be structured specifically for small- and medium-size businesses. The tax bill, as I understand it, and I would readily acknowledge not being expert in it, does not seem to me in any fashion to get to the heart of what I believe to be America's competitiveness problems, which is that we consume too much and save too little.

It is not going to encourage greater savings or greater investment. It does permit, if not, indeed, encourage, the continuation of the status quo.

Mr. **Mazzoli**. Thank you.

In the periphery of my vision, I noticed there was some reaction perhaps in the middle of the table, by Mr. Rennie and Mr. Campbell, and others, about the question of tax policy and the whole idea of competitiveness.

Mr. **Rennie**. Maybe approaching it a little differently just to give you an idea of what we are up against.

I am constantly being approached by the Industrial Development Authority in Ireland to put a manufacturing plant in Ireland. Now, if I were to do that, they would, first of all, establish a maximum of 10-percent corporate income tax on that group through the year 2000, and with the depreciation allowance they give, basically, you would probably not pay more than 5 percent.

They give you a 60-percent grant against capital equipment. They give you a 100-percent grant against training of Irish workers, including bringing Irish workers to the United States, if necessary, temporarily to train them and they give you a 50-percent credit, essentially a grant, against R&D.

Now, here is a business proposal that I have, and I am trying to make a decision as an American company——

Mr. **Mazzoli**. Stay here or go there.

Mr. **Rennie** [continuing]. To stay here or go there. And industrial development authority, Scotland, and the equivalent groups in Scotland, England, Holland——

Chairman **LaFalce**. Did I not read that Ireland, in particular, is targeting the small business sector in the United States as opposed to large business?

Mr. **Rennie**. I would not be surprised. I mean, IDA Ireland has done an absolutely super marketing job. They have established relationships throughout the country with small business groups, and they are very aggressive, and they have brought over—I think the last number I heard was $3 billion worth of industry to Ireland.

So, despite all their problems and despite their unemployment, they are working very, very hard. So, all I am getting at is, you see, they have a real priority. They have set a priority there, and they are putting their money where their mouth is.

Mr. **Mazzoli**. Mr. Chairman, my time may have expired. Just tell me when it is.

Mr. **Donley**. Can I respond to just one sentence?

Mr. **Mazzoli**. Sure.

Mr. **Donley**. The Irish IDC did target our company, the 237th largest corporation in the United States, and we have established a business with these supports just outside of Dublin along the line Jack said.

So, I think they are targeting large corporations as well.

Mr. **Mazzoli**. As well as small.

Mr. Campbell, maybe you could respond.

Mr. **Campbell**. Yes; we have seen a lot of that activity this year, and, actually, through the international trade committee of the Small Business Association of New England [SBANE]. In January, for example, we had representatives from the Port of Hamburg visit the Boston area and they put on a complete presentation at one of the hotels in Boston.

Just getting back to what you were talking about, tax incentive, though, I think just in terms of the very grass roots level of getting our very basic industries—I mean, you go into small companies in Switzerland and Germany, there may be half a dozen people in there and yet there is almost always one person that is cognizant of all the export regulations.

We have to have that training. We have to have that training.

Mr. **Mazzoli**. Do you see a Federal role in that?

Mr. **Campbell**. The Federal role I see is getting it so there is an incentive there from tax purposes so that we get these people, so that we get industry involved, and get them to train these people so that they can competently perform the day-to-day trade routines and actively consider international trade as part of their ongoing business, not just something that they occasionally do.

For example, I have worked with companies as a consultant, where there has been 25 export inquires waiting to be handled. What are we going to do with this? How are we going to help firms become competitive? They do not know how to handle international trade documentation.

Mr. **Mazzoli**. Well, I thank you, gentlemen. My time has expired, but let me just say again to Mr. Donley, despite what Billy Joel says, I am sure that Allentown is a great city.

Mr. **Donley**. You are right.

Chairman **LaFalce**. Mr. Hefley.

Mr. **Hefley**. Thank you, Mr. Chairman.

This is a distinguished panel, and I have enjoyed it thoroughly. Sorry I did not get in on all of it. We have had some excellent witnesses over the last couple of weeks on this subject of our competitiveness abroad and trade and so forth, and you have made a lot of good suggestions.

I guess, though, I would like for you to speak a little bit to what we should do about the protectionism on the part of other countries, that no matter what we do, no matter how much more aware we become of the trade regulations and ways to do it and so forth, we still cannot get our products in some of these countries.

Japan is a perfect example of it, I think. They will tell you that, well, we believe in free trade, but American products are shoddy and they are not well designed and engineered and the sophisticated Japanese consumer just does not want American products. But that is simply not true.

You take, for instance, American contractors that have great experience in heavy earth-moving projects and, yet, they are completely shut out of the $8 billion Osaki Airport project. Cannot even go in and bid on that project, I understand.

American medical equipment leads the world, but you cannot sell it in Tokyo. And its the same whether you are talking about oranges, or cigarettes, or chocolate, or bourdon, or beef, on which I think there is a 125 percent tariff. They have even made a decision recently to produce their own fighter plane, which they could buy off the line in America for about half the cost, and when you are talking billions of dollars for a fighter plane, that would help tremendously in our $59 billion trade deficit with the Japanese, and yet they are going to produce it.

It seems to me that they believe in free trade when we are talking about automobiles, but not fighter planes. So, what do we do about that? I do not want to be protectionist. I believe in free trade, but I am getting darn mad at the Japanese who will steal our technology and reproduce it but think we are shoddy in our products and will not let us compete over there.

Anybody that has a comment? Yes?

Mr. **Rennie**. I would like to respond. First of all, Mr. Hefley, I think that there is an excellent presentation that I saw, put on by a professor at the Harvard Business School that profiles countries around the world with the view toward looking at them relative to the underlying theory of trade of comparative advantage; and it is very interesting. The basic idea being that those things we are good at, that we have raw materials for and so forth, those are the sorts of things that typically a country will export quite a bit, and then there are other things that we are not so good at and we import, maybe some raw materials in our case.

If you look at the various profiles of the countries around the world, every country but one has pretty much the same profile, which is that if you put them in a vertical column, list all the various products and just after gathering the statistics you go from top to bottom on those that we are best at versus those that we are worst at, you develop very much of a U-shaped curve, showing that those things that countries are good at and have the comparative advantage, they export a lot of, and then those things they are poor at, they import a lot of.

The only anomaly in the whole world of all the countries that we saw was Japan, where those things that they are very good at and have the comparative advantage, they export tremendously, and those things that they are not very good at, they do not import.

So, you have a half a curve basically——

Chairman **LaFalce**. Let the record indicate that Mr. Rennie is referring to the studies of Professor Bruce Scott.

Mr. **Rennie**. Bruce Scott. Yes; thank you, Mr. Chairman.

And, so, it is kind of revealing, and the only thing I would say is that naturally, we get irritated, too, but the thing is that it may be dangerous to judge our total international policy based on the way that Japan operates because, clearly, they are an anomaly at least in this presentation, in this study.

On the other hand, I think there is great sentiment that while there is not, I think, broad sentiment for protectionism in the small business sector across the country, there is a good sentiment toward really pushing the fair trade idea. And if, to a certain extent, as I mentioned, enlightened reciprocity should be employed in which, in fact, if someone is not playing the game, I think there is a lot of sentiment to begin to formulate some kinds of reciprocal actions to take that into account.

But there is no doubt about it that Japan is special. I mean, in Japan, there are all kinds of things: For example, I am a defense contractor. There are all kinds of things that could be sold there. You cannot deal directly with the Government; you have to go through Japanese intermediaries. Well, we certainly do not have this barrier in this country. A Japanese seller can come directly in and market the Government.

So, there are some definite things with respect to Japan, But, I think there is very strong sentiment in the fair trade. I guess I would tend to caution not to base our trade policy on just Japan because Japan should be dealt with almost separately.

Mr. HEFLEY. Then, would you agree that we ought to have some weapons in our arsenal at least to deal with those anomalies like that?

Mr. RENNIE. I think we should have the weapons, but if it is in the case of the President taking action in certain areas, I would tend to favor a policy which has some kind of reasonable out-clauses so that if he really feels through other information he has that an action would be detrimental to the United States overall, he would have some ability to impose his judgment on that.

So, that would be my view of it anyway.

Mr. HEFLEY. Thank you.

Chairman LAFALCE. Mr. Olmer, did I detect your desire to comment on that?

Mr. OLMER. I rather think not, Mr. Chairman. It is a question the response to which could go on for a long while. I agree with the underlying concept that it is necessary for the U.S. Government, the administration principally, but supported by the Congress, be given the wherewithal and the means and strategy for not permitting American exporters of goods and services to be dealt with unfairly.

But I also believe that our problems have become so large that all the open markets in the world will not make but a rather insubstantial contribution to their resolution, unfortunately.

Chairman LAFALCE. And do you view those as the so-large problems? Theoretically, we have reduced the value of the dollar, at least with respect to certain major currencies, and the yen in particular, and it was for so long a position of the administration that that was the primary reason behind our trade deficit. Now you seem to be suggesting that even if, given that fact and despite the fact that there are closed markets abroad, there are other causes to our problems.

This is an argument that I have been making over the past 4 or 5 years. I do not know that it has been made by representatives of the Reagan administration. So, what is it that you are possibly about to say?

Mr. OLMER. Well, with your help, I might get it all out.

Mr. MAZZOLI. Volunteer.

Mr. OLMER. The economists in our midst explain the absence of marked improvement in the trade balance despite the reduction in the value of the dollar by saying that the J-curve is getting a lot larger than we assumed at the beginning.

Chairman LAFALCE. Well, I initially heard the J-curve had a 6-month life. Then, I heard a 12-month life, and then an 18-month life, and now I am told it has a 2-year life. This is quite a curve.

Mr. OLMER. Well, what I believe the issue will come down to is whether or not the United States is prepared to accept a lowered standard of living, which is what inevitably a lowered valued dollar will mean.

We cannot continue to sustain large trade current account and budget deficits. It simply cannot be, and eventually the account will balance. The question is over what period of time and at what cost.

We have seen an enormous cost to the heartland of American industry, and I believe we are going to see it get much worse before it gets better. The answer will not be provided through opening foreign markets; it will not be provided through getting new SIC codes for services. The $44 billion in the services account is about 80 percent comprised of tourism and shipping, and passenger fares. Roughly $3.5 billion of surplus in that area is attributable to the entire calculus of engineering consultants, software, telecommunications, and consulting in other areas.

We are going to have to provide that surplus through manufactured exports, pure and simple, and the question is at what price will they be sold abroad, and that means that the dollar is probably going to have to come down a good deal further than it is at present—an unhappy prospect.

I do not believe that the value of the dollar will be within the power of the Fed and the administration to control if and when it gets on a roll downward. We have seen evidence in the last few months where intervention by Germany and Tokyo in the neighborhood of $20 billion, had no affect on the downtrend in the dollars value.

What does? Well, I am not an economist, sir, I am an honest man, and I do not read entrails. I do not know.

Mr. MAZZOLI. How about tea leaves?

Well, Mr. Chairman, very interesting. I do not understand all this esoteric about money and the values and so forth, but——

Chairman LAFALCE. You do not have to understand it. Otherwise, hardly a soul would be talking about it.

Mr. MAZZOLI. I remember the days when our dollar was very strong and people were yelping and screaming about the strong dollar. Except that the strong dollar is, at least in part, a kind of measurement of the idea of the attitude of Nation, of the world toward that Nation, and that was very optimistic—a strong Nation on the move, vigorous, dynamic.

Then, all of a sudden, we said, hey, that is a bad scene. So, we say, well, let us just take the bottom out of the dollar and let it just go over the cliff and that is going to make a lot of good things as far as exports and bad things as far as imports, and that is what we need. Except that if you use the measurement of the dollar as in part the attitude of the Nation toward the world and vice-versa, it is a bad thing.

Now, all of a sudden, this morning, driving into the office, the yen was at its highest value ever since post-World War II toward the dollar. People are pulling their hair out by the handfuls and jumping off cliffs and everything else.

I guess the question is, basically, if you say, and it may be general wisdom, that you are not going to solve the imbalance by just dropping the value of the dollar in the portent of that, the implications from that are so fierce, maybe it is time to quit flat out and try something else, even if it means putting up barriers or doing things that this Nation has never done before. I do not know.

I mean, is there any reaction to that?

Mr. OLMER. Well, not merely Mr. Gephardt's proposal has been kicking around but lest we presume we are really a nation which observes free trade to the nth degree, we have got the market sharing arrangements, as you say, up to the gazoo, as a former colleague from another body used to say.

Mr. MAZZOLI. That is right.

Mr. OLMER. In a different context. We have got steel and textiles and automobiles and what have you. I am not arguing whether we should or should not have them, but we do have them and that may be the portent of the future, to make them stricter. I think it will have a lot of bad side effects, but I do believe the problem is so serious and will not be solved by opening up foreign markets more than they are already opened up, not that we should not try. Services are the wave of the future, and the future of high technology is supremely important for a lot of different reasons. Absolutely. But it is not going to deal with the humongous proportions of our trade, current account and budget deficit.

Mr. DONLEY. I could give you a brief example from our own current experience, Mr. Chairman.

We believe the lower dollar makes a difference and we are now building, in our shops in Wilkes-Barre and Allentown, tens of millions of dollars of cryogenic equipment going to Japan. The American technology is believed to be superior. The Japanese believe it and we believe it, but this is the first time in 20 years, with the dollar where it is now, that we have been able to supply that market.

However, and I am sorry Mr. Hefley left, we do not have the same access to that market as they have to our market. One of the ways that it is restricted is that there are certain policies in Japan that require us to submit details of the internal characteristics of our fractionating columns. They are not patented, but they represent trade secrets that cost us a lot of research and development to provide, and we are not prepared to give those away to anybody so that they can be duplicated at no cost.

The only way to get around it, therefore, is to form a Japanese company with a Japanese partner which would export from the United States to Japan. Although we would keep the jobs in the United States, with such a partner, we would lose half of the profit to our Japanese partner.

I think we have to come down on Japan very hard and restrict those opportunities they have to import here unless they give us equal access to their markets and this is far preferable to putting up protectionist barriers. We set up this system under General MacArthur. Mr. Dodge from the First National Bank of Detroit, an economist from the University of Chicago, set up this system to enhance exports from Japan and they have become prodigiously prosperous over the last 40 years. They are not going to give that up unless we get very, very tough with them. I think that is what we have to do and I think it depends on the United States Government.

Let us face it, we in the business community, are a little chickenhearted. We do not want to lose the next order by coming down too hard on Japan. So, we have to turn to our Government to provide us the level playing field that their Government provides to their manufacturers.

Mr. MAZZOLI. Can I ask just one last question? I promise to shut up, Mr. Chairman.

Assuming we did something like what Mr. Donley suggested and Secretary Olmer did, is there any legitimate fear on the part of the Japanese that America, being so big and so tremendously tough and one of the first of the great mercantile nations, would just overwhelm Japan and put them back in the ashes of World War II again?

I mean, is there any legitimate fear that we could, if there is true reciprocity, just overwhelm them just as if there were true reciprocity with emerging nations that we could just have another Sherman march to the sea? I mean, is that something for them to legitimately worry about?

Mr. DONLEY. No.

Mr. MAZZOLI. Mr. Rennie, Mr. Campbell, gentlemen?

Mr. DONLEY. No, it is not. Unemployment is higher, and, of course, they are concerned, but they are in a box. They have made a strategic mistake, perhaps unavoidably.

In any marketing program, it is unwise to get too many eggs in one basket, to depend too much on any one customer, and Japan's prosperity does depend too much on the American markets. So, if they lose the American market, they are in trouble, politically and economically. But I think that fairness is fairness. We have got to go a long way from where we are before the fair trade is really in existence between the United States and Japan.

Mr. RENNIE. I think that one of the things that holds back the U.S. Government is the fear that if we took a very tough line with Japan that they could use their, what I think has come to be, sad to say, ultimate card, which is that they just will not fund a third of our deficit anymore as they did last year.

I mean, they buy something like 30 percent of all the U.S. bonds and that means a hell of a lot of Japanese money flows into the country and has so far helped prop up the $200 billion deficits. I think that is what really makes the policy-makers in Government hesitate, although they know that Japan may deserve it, to be treated damned toughly, but they are really worried about the fact they may pull their money out and start putting it in Deutschmarks or something like that.

Mr. MAZZOLI. Anyone else venture—because I know some of the problems we had with the Caribbean Basin initiative. We want to do something so that the people in the Caribbean Basin can find opportunities in their home country. It is better than emigrating to the United States.

On the other hand, when you start setting up a market or providing for them some equal access, then, of course, it means American workers are hurting, so we do not get very far, and the people continue to emigrate and the continued lack of opportunities in those home countries cause uprisings and tensions that produce political conflagration and, so, this trade thing has a lot of implications into the stability of governments and everything else.

But, Mr. Campbell and the other people?

Mr. CAMPBELL. I would take some issue with Jack just on that last statement, at least from the congressional point of view, because my feeling is that where else are they going to reinvest their money back. I mean, there is not another country in the world where they can really—there is West Germany—but there is nothing of the size and of the potential of the magnitude really to do it.

Let us see. There was one other thing. I lost my track of thought on that.

Mr. MAZZOLI. Talking about some of the third world or some of the pressure, the equal access or reciprocity. Well, anyway——

Mr. CAMPBELL. I do think just in very general terms and again bringing it down to small business, I do think overall just in ongoing contact with Japanese as such, there tends to be somewhat of an intimidation and a xenophobia as of doing any kind of business with them just in the presentation of the nature of it.

Mr. MAZZOLI. Thank you.

Chairman LAFALCE. Ms. Littlejohn?

Ms. LITTLEJOHN. Thank you. If I could answer that, the National Association of Women Business Owners had a trade mission to Tokyo and Osaki this past summer, a 2 ½- or 3-week trade mission, and we had worked very closely with Department of Commerce in developing particular market sectors that we thought we could go after, and had zeroed in on medical and health care services where we are again quite a few years ahead of them.

The extraordinarily successful trade mission and very much to my surprise, we had been very reluctant to even consider going to Japan because we had thought there might be some real barriers for women business owners dealing with the male Japanese business community, but we had done a very, very intensive cultural training program for all of the trade mission people before they went, and we have developed a number of followup trading relationships with Japanese businessmen who have been coming back to the United States quite a bit.

We have particularly developed a strong relationship with our North Carolina chapter, where we are dealing both with some manufacturing and some service-type things.

At any rate, as we have gotten to know these gentlemen much better and they are working quite closely with us now, they also indicated that they had major difficulties working with the American business style or, as they viewed it, more the male business style, that our people were not attuned to their cultural practices, their modes of civility, the rituals that you have to go through doing business in Japan, and I think it is much more complex than just putting it in a closed market kind of context.

I really think we have to do our homework on that front if we are going to crack some of those cultural barriers.

Mr. MAZZOLI. I promise nothing more, but I understand, and maybe somebody could put the numbers, that there are something like hundreds of thousands of Japanese who speak English fluently and maybe 10,000 Americans who speak any Japanese whatsoever. The majority of American executives in Tokyo need interpreters, they cannot speak the language. That obviously is one great deficiency because it is obviously so much easier and they feel so much more flattered if you could speak their language as we feel flattered and as, frankly, the presentations are more effective in your own tongue.

So, I think one of the many things that ought to be done is to somehow promote in the American educational system the study of foreign nations and languages, but perhaps particularly Asian nations as they are now coming so much to the forefront in world trade—Chinese, Japanese, so forth.

But, anyway, I thank you for bringing that up.

Ms. LITTLEJOHN. I think that is, in fact, a critically important point. I have lived in Tokyo for 3 years, a number of years ago, and it would be very difficult for most Americans to learn Japanese quite well. It is a very tough language, but there are just common courtesies. I mean, there would be a basic 100 words that you could probably learn and appropriate civilities and modes of address, the right timing.

I mean, there is a real ritual to how business is done in Japan, and by our not knowing that, it really puts us at an extreme competitive disadvantage because they really consider us practically barbarians if we do not know how to do that.

We spent time before our trade mission just in marathon training. Everybody had to read particular books, particular publications. Everybody was trained on timing, the right modes of address, and while we thought that we were not going to be well received because of being female, in fact, after we had been working with these gentlemen for almost a year, we have been getting feedback that they have never had a finer trade mission, and they had never worked with people who were more attuned to how to deal with business with them.

We had a $1 million contract signed a week after the trade mission.

Mr. MAZZOLI. Proves out the point. Common courtesy is never a bad deal.

Thank you, Mr. Chairman.

Chairman LAFALCE. Ms. Littlejohn, gentlemen, I want to thank you very much for your contribution to today's hearing. We will have to, though, now adjourn. Thank you.

[Whereupon, at 12:35 p.m., the committee adjourned, subject to the call of the Chair.]

APPENDIX

Statement of the Chamber of Commerce of the United States

ON: THE TRADE AND INTERNATIONAL ECONOMIC POLICY REFORM ACT OF 1987

TO: SUBCOMMITTEE ON TRADE
HOUSE COMMITTEE ON WAYS AND MEANS

BY: WILLIAM T. ARCHEY

DATE: FEBRUARY 18, 1987

The Chamber's mission is to advance human progress through an economic,
political and social system based on individual freedom,
incentive, initiative, opportunity and responsibility.

The U.S. Chamber of Commerce is the world's largest federation of business companies and associations and is the principal spokesman for the American business community. It represents approximately 180,000 businesses and organizations, such as local/state chambers of commerce and trade/professional associations.

More than 91 percent of the Chamber's members are small business firms with fewer than 100 employees, 58 percent with fewer than 10 employees. Yet, virtually all of the nation's largest companies are also active members. We are particularly cognizant of the problems of smaller businesses, as well as issues facing the business community at large.

Besides representing a cross section of the American business community in terms of number of employees, the Chamber represents a wide management spectrum by type of business and location. Each major classification of American business--manufacturing, retailing, services, construction, wholesaling, and finance--numbers more than 11,000 members. Yet no one group constitutes as much as 29 percent of the total membership. Further, the Chamber has substantial membership in all 50 states.

The Chamber's international reach is substantial as well. It believes that global interdependence provides an opportunity, not a threat. In addition to the 56 American Chambers of Commerce Abroad, an increasing number of members are engaged in the export and import of both goods and services and have ongoing investment activities. The Chamber favors strengthened international competitiveness and opposes artificial U.S. and foreign barriers to international business.

Positions on national issues are developed by a cross section of its members serving on committees, subcommittees and task forces. Currently, some 1,800 business people participate in this process.

STATEMENT
on
THE TRADE AND INTERNATIONAL ECONOMIC POLICY REFORM ACT OF 1987
before the
SUBCOMMITTEE ON TRADE
of the
HOUSE COMMITTEE ON WAYS AND MEANS
for the
U.S. CHAMBER OF COMMERCE
by
William T. Archey
February 18, 1987

Mr. Chairman and Members of the Subcommittee, I am William T. Archey, Vice President, International, of the U.S. Chamber of Commerce.

We appreciate the opportunity to testify on H.R. 3, the Trade and International Economic Policy Reform Act of 1987. We applaud the thoroughness with which you are addressing the very complex issue of American trade performance and our economic competitiveness. While we are pleased with many of the constructive suggestions you have recommended in this legislation, we do have serious problems with certain other provisions. And may I add that we especially appreciate the cooperation of both members and staff in working with the U.S. Chamber as well as our 56 affiliated American Chambers of Commerce abroad.

As you requested, my testimony today will focus on Titles I and II of H.R. 3. But there are many other important elements in this measure, and I have included a summary of the Chamber's current position on a host of these provisions as an attachment to this statement.

The U.S. Chamber believes there are three basic objectives to the formulation and execution of international trade policy. They are:

1. To improve the ability of U.S. firms to compete internationally by pressing for the elimination of foreign tariff and non-tariff barriers to U.S. trade and investment.

2. To improve the ability of U.S. companies to compete effectively abroad by eliminating domestic disincentives to U.S. international business performance while actively proposing and supporting policies for export promotion.

3. To improve the ability of U.S. firms to compete domestically by providing effective domestic recourse to foreign unfair trade practices and injurious imports, while ensuring U.S. consumers access to fairly traded goods and services.

We view H.R. 3 as a starting point towards achieving these objectives. The Chamber of Commerce has taken the above objectives and defined a detailed program for accomplishing them. We have recently restructured its International Policy Committee to focus on these objectives, and have formed three separate subcommittees, each of which is responsible for one of the objectives.

Mr. Chairman, the enactment of constructive trade legislation this year can contribute significantly to correcting some of our trade related problems. But we must be realistic as to what it can and cannot do. There are major macroeconomic issues, such as the budget deficit, third world debt, and growth rate differentials and exchange rate instability among the industrialized nations, that present serious problems which are not amenable to solution through trade legislation.

However, the Chamber of Commerce does feel that there is a need for trade legislation that could have a positive impact on America's international trade competitiveness. New trade legislation as well as the aggressive implementation of existing trade law can provide important incentives for U.S. business to export, remove disincentives to export, and aggressively combat the unfair practices of our trade partners without becoming protectionist.

In fact, on January 16, U.S. Chamber Chairman Edward Donley wrote the President, urging him to work with the Congress in the development of constructive trade legislation. He also made some specific suggestions, which are included in his letter, a copy of which is attached.

In that regard, H.R. 3 includes a number of positive provisions which are consistent with our objectives, including:

- strengthened telecommunications market access provisions;
- strengthened intellectual property rights protection;
- new trade agreement negotiating authority;
- mandatory retaliation against foreign unfair trade practices;
- clarification of the Foreign Corrupt Practices Act;
- improved procedures for the Export-Import Bank.

However, the bill also includes a number of objectionable provisions which would undermine our position in the world trading system. Two of those provisions would include:

- The so-called "Gephardt amendment", which would mandate U.S. retaliation on the basis of a unilateral determination that other countries' trade surpluses are "excessive and unwarranted." This amendment would likely violate U.S. GATT obligations, provoke swift retaliation, probably raise prices and could create shortages in affected sectors and ultimately reduce trade opportunities for U.S. companies.

- Inclusion of "internationally recognized workers' rights" (such as rights to association, organization, collective bargaining, prohibition on forced or compulsory labor, minimum employment age, and "acceptable conditions" with respect to minimum wages, work hours and occupational safety and health) as a condition to be considered by the Administration in taking retaliatory action; such a condition is highly arbitrary and would be unworkable.

Mr. Chairman, let me now turn to a more detailed discussion of some of the major provisions of H.R. 3 as they appear in the bill, and the Chamber's view of each.

Section 301 (of the Trade Act of 1974)

The Chamber strongly supports effective use of Section 301 to achieve the elimination of foreign barriers to U.S. trade and investment. Even though such barriers constitute a relatively small share of our trade deficit, their persistence reflects a widespread belief among our trading partners that the United States is reluctant to do what needs to be done to protect its legitimate interests in a fair and open trading system. Furthermore, many of our members, including some of our most successful exporters, complain that other countries exclude U.S. access to their markets knowingly and in violation of bilateral and multilateral trade agreements, but with little fear of adverse U.S. government action.

We applaud the U.S. administration's recent actions under Section 301 to improve U.S. access to foreign markets. In our view, these actions represent an important beginning of a newly assertive U.S. trade policy that will send the message to our trading partners that the U.S. will no longer play the fool while other nations unfairly reap the benefits of world trade. However, as useful as these actions may have been, they are not enough. As powerful a statute as Section 301 is, it does not now provide sufficiently certain recourse against foreign unfair trade practices. For this reason, the Chamber strongly supports those provisions of H.R. 3 which would mandate retaliation against foreign trade practices that violate international trade agreements. At the same time, the Chamber has performed an analysis of Section 301 enforcement in which we have examined the timeliness and outcomes of investigations and dispute settlement efforts undertaken under that law. In addition, the Chamber is currently surveying those companies and other organizations that have filed Section 301 petitions. The results of that survey will help us to determine whether additional changes regarding timetables, administrative discretion or other matters are warranted. We expect to reach some preliminary conclusions early in March.

H.R. 3 defines three new practices as actionable under Section 301: injurious export targeting, violations of internationally recognized workers' rights, and toleration of cartels. The Chamber supports use of Section 301 as a vehicle for responses to injurious export targeting. We oppose including denial of "internationally recognized workers' rights" as an actionable practice. The U.S. itself has not ratified any of the International Labor Organization (ILO) conventions which correspond to these proposals; unilateral establishment of such a standard in trade law is not only arbitrary, but adds new ambiguity to the trading system which could also invite retaliation from countries who view their own labor standards as superior to our own.

H.R. 3 would require retaliation against countries maintaining "excessive and unwarranted" trade surpluses with the United States if bilateral negotiations to reduce those surpluses failed to reach specific results within a specified time period. We note that there are "waiver" provisions which include reference to debtor nations and the U.S. "national economic interest". Nonetheless, the Chamber opposes this provision. First, the definition of an "excessive" trade surplus (a non-petroleum export/import ratio of 175%) is arbitrary. Such a ratio may simply reflect a nation's comparative advantage and could exist without the perpetration of an "unwarranted" trade practice. The definition of "unwarranted" practices is itself so vague that it would invite retaliation against other nations which are not engaged in "unwarranted" practices but have competitive, trade-oriented industries. Such U.S. retaliation could easily lead to counterretaliation against U.S. industries that are not engaged in unfair trade practices.

Section 201 (of the Trade Act of 1974)

The Chamber continues to support the use of fair trade statutes to provide temporary relief to seriously injured domestic industries. We encourage the Congress to ensure that revisions to the current statute retain the legislative intent of industry adjustment and that the granted relief should be temporary in order to facilitate this adjustment to import competition.

The Chamber endorses reforms which require the ITC to estimate effects of relief on U.S. consumers and domestic competition; this should allow the President to more effectively consider the tradeoffs between providing relief to the injured industry and the resulting costs to other elements of the economy.

Efforts to strengthen the link between relief granted and action taken toward industry adjustment are also important and constructive. Proposed reform in H.R. 3 to establish procedures for an industry adjustment advisory group to prepare an industry adjustment plan are unlikely to result in the group's collective agreement on an adjustment plan within the limited statutory deadlines. Furthermore, the Chamber has serious reservations about the advisory group, as it may be the precursor of an industrial policy giving government a greater involvement in economic decision making.

H.R. 3 would provide for expedited consideration of Trade Adjustment Assistance (TAA) petitions and establish a Trust Fund financed by tariff revenues and auctioned quotas to fund retraining programs under TAA. The Chamber believes that one consolidated program for all displaced workers should be established, and in this vein, supports the President's recently proposed worker adjustment program.

We feel that the TAA program is duplicative, does not adequately stress worker retraining, and has instead emphasized income maintenance alone. We have also been opposed to the imposition of additional import fees to fund such programs; such measures would be GATT inconsistent.

Antidumping and Countervailing Duty Statutes (Tariff Act of 1930)

The Chamber recognizes the seriousness of persistent dumping and subsidy practices by foreign trading partners.

Diversionary dumping, in particular, has increasingly been the cause of concern to industries injured by such unfair practices. While legislative solutions to this problem could be constructive, they would be extremely difficult to administer. The Chamber's International Policy Committee sought to address this issue, and while it could not agree on a constructive, rational approach, it did recommend that this issue be addressed in multilateral trade negotiations. The complexity involved in actually defining "diversionary dumping" requires cooperation with our trading partners and avoidance of premature, unilateral solutions which may be in violation of our obligations under the GATT.

The right of private action has also received considerable attention in the current trade debate. While the Chamber has formally taken no position on this issue, we do recognize the fact that antidumping and CVD investigations are not punitive statutes, in our domestic law nor in the multilateral codes. The International Policy Committee is presently addressing this issue and will have a position shortly.

H.R. 3 also establishes natural resource pricing practices as subsidies if not available to U.S. firms at the same price as it is to the other country's domestic firms. The Chamber takes no position on this issue.

Section 337 (of the Tariff Act of 1930)

With intellectual property piracy costing U.S. companies an estimated $8 billion to $20 billion a year, the Chamber is committed to modernizing applicable laws. We support the key House provisions in H.R. 3, which address this issue.

Section 337 of the Tariff Act of 1930 presently gives the International Trade Commission (ITC) the general power to exclude imports when the importer engages in "unfair methods of competition or unfair acts." The law has been used to restrict importation of pirated products, but it needs to be strengthened by eliminating the injury test. The law was not designed specifically to protect intellectual property rights; rather it requires a complaining party to show that the imports threaten an efficient and economically operated domestic industry with destruction or substantial injury, only then can relief be granted. We support the removal of such an injury test; that the articles infringe a patent or are made abroad by the unauthorized use of a process that is patented here should be sufficient reason for exclusion.

We also support a change in the law that would require the ITC to act promptly on requests for relief, pending the final resolution of a complaint. In cases in which a key shipment of infringing goods is en route or a critical selling season is approaching, the failure of the ITC to act promptly inflicts harm on the intellectual property owners that is not easily remedied.

Section 232 of the Trade Expansion Act of 1962 (Imports Affecting National Security)

H.R. 3 would shorten from one year to 90 days, with one 90 day extension, the deadline for completion of Commerce Department investigations under Section 232 (pertaining to imports which allegedly threaten national security). In addition, the time period for a Presidential decision with respect to the results of the investigation would be limited to 30 days after receiving the report of the Secretary of Commerce. The Chamber strongly opposes this provision. As someone very familiar with the investigation process under Section 232, I can tell you that 90 days is far too short a period in which to make an adequate factual determination. We understand the committee's concern over the problems associated with enforcement of Section 232, but the issue is to require the President to make a decision, not the length of time it takes to complete an investigation. In our view, the bill should limit its changes to requiring the President to act, one way or the other, within a reasonable time from receipt of the 232 investigation report.

Telecommunications Products and Services

We support most features of the telecommunications provisions of H.R. 3, which we believe will go a long way towards solving many of the problems in this industry. These include: Giving a strong Congressional mandate to the President to negotiate multilateral and bilateral agreements that would provide fully competitive opportunities to worldwide telecommunications markets; establishing reasonable standards by which equivalent market access is determined; authorizing the President to offer incentives to other countries to reduce their trade barriers; including access of U.S. foreign subsidiaries in judging overall access to these markets; enabling the President to investigate individual company grievances when appropriate petitions are filed; mandating the President to monitor the results of negotiated agreements or self-initiated liberalization; relying upon existing divisions of responsibilities among federal trade agencies; and being compatible with the General Agreements on Tariffs and Trade (GATT).

We do oppose the provision of the section that mandates the President to retaliate if no agreement is reached as a result of negotiations.

Revision of Standards Applicable to Nonmarket Economies (Market Disruption)

The U.S. business community generally agrees that current antidumping law regulating nonmarket economy (NME) imports is grossly inadequate. The surrogate country/constructed value approach for determining dumping from NMEs has created tremendous confusion on the part of government regulators, importers, and domestic industry alike. In addition, Section 406 of the Trade Act of 1974 has not been a useful tool in the present import administration process.

We believe that both laws should be replaced by a single new law that permits an industry or sector within an otherwise NME to be judged market-oriented for purposes of antidumping duty investigations if, for example, that industry or sector is able to function reasonably independently of state control in establishing production levels and product price determinations.

The Chamber maintains that there is no equitable and predictable way for measuring the fair market value of NME imports. As such, the Chamber believes that an injury determination should be the sole requirement for import relief in the case of NME products.

Under our proposal, if the ITC finds injury, the Office of the USTR would be empowered to negotiate within a reasonable period an arrangement with the NME, through price increases and/or quotas, to remedy the injury. If the USTR fails to reach such an arrangement with the NME, the USTR still would have the authority to recommend the ITC a remedy for domestic industry.

Trade Negottiating Authority

We are pleased that the GATT signatories agreed to a new round of multilateral trade negotiations at Punta Del Este last September. We are encouraged by the success of our negotiating team in having such issues as intellectual property, services, agriculture, and investment included in the forthcoming Uruguay Round.

In general, we agree with most of the provisions in H.R. 3 with respect to trade negotiating objectives and authority. In general terms, we support the negotiating objectives in the bill, the extension of tariff and nontariff negotiating authority, as well as fast track authority.

However, we oppose that provision which makes such negotiating objectives mandatory for our negotiators; and we also oppose the concept of forcing the President to convene an international monetary conference before the United States can proceed to negotiate nontariff barriers.

You may be interested in our priorities, which are: (1) to strengthen the disciplines of the international trading system, and to seek further reductions of nontariff and tariff barriers, we must review issues such as Most-Favored-Nation Treatment, permissive customs unions and free trade areas, safeguards, dispute settlement, and government intervention in trade; (2) to examine GATT machinery and the role of its Secretariat in order to improve its performance; (3) to help GATT adapt to the emerging needs of services, investment and intellectual property rights and agricultural issues; (4) to review the linkages between trade and monetary matters; (5) to assist developing countries to assume a more active and responsible role within the world trading system; (6) to secure maximum public support in order to improve present trading rules and institutions and to provide directions for solutions to other new or yet-to-emerge problems; and (7) to seek renewed Presidential negotiating authority from the U.S. Congress.

Finally, we also support that provision of the bill which extends our negotiating authority with Canada for five years.

Mr. Chairman, that concludes my statement. I will be glad to respond to your questions.

TRADE AND INTERNATIONAL ECONOMIC POLICY REFORM ACT OF 1987

Comparison of Major Provisions

TITLE I--TRADE LAW AMENDMENTS

Subtitle A. Enforcement of United States Trade Agreements Rights and Response to Certain Foreign Trade Practices

SECTION 301 (Trade Act of 1974): UNFAIR TRADE PRACTICES

H.R. 3 Provision	U.S. Chamber of Commerce Position
o Transfers authority to initiate Section 301 cases from President to U.S. Trade Representative (USTR); President retains final decision-making authority.	o Opposes transfer of Section 301 decision-making authority from President to USTR.
o Makes Section 301 retaliatory action mandatory if foreign countries violate an international agreement or commit other "unjustifiable" practices; Retaliatory action against "unreasonable" or "discriminatory" practices remains discretionary.* (Mandatory action may be waived under certain circumstances, including likely adverse impact on U.S. "national economic interest").	o Opposes mandatory retaliation except in cases of trade agreement violations. Supports waiving action if retaliation adversely affects other U.S. interests.
o Requires considering impact of Section 301 actions on U.S. agricultural exports (counterretaliation).	o No position.
o Makes denial or elimination of Generalized System of Preferences benefits an option for Presidential action.	o No position.

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*Definitions:

Unjustifiable: refers to acts, policies, or practices which violate or are inconsistent with U.S. international legal rights, such as denial of national or most-favored-nation treatment, right of establishment, or protection of intellectual property rights.

Unreasonable: refers to any act, policy, or practice which, while not necessarily in violation or inconsistent with international legal rights of the United States, is otherwise deemed to be unfair and inequitable.

Discriminatory: includes, where appropriate, any act, policy, or practice which denies national or most-favored-nation treatment to U.S. goods, services, or investment.

o	Adds three new practices as subject to Section 301 action: injurious export targeting (retaliation is mandatory), violations of internationally recognized workers rights, and toleration of cartels.	o	Supports use of Section 301 as vehicle for responses to "targeting", but opposes mandatory retaliation unless a trade agreement has been violated. Opposes denial of internationally recognized workers' rights as basis for 301 action; no position on toleration of cartels as basis for 301 action.
o	Requires USTR to self-initiate Section 301 cases if information in annual "National Trade Estimates" (nontariff barriers) report meets certain criteria.	o	No position.
o	Requires Section 301 case initiation if bilateral trade surpluses are "excessive and unwarranted"; calls for bilateral talks on measures to reduce surpluses by 10% per year and mandatory retaliation if talks (or measures) fail. There are waiver provisions.	o	Opposes mandatory retaliation in absence of a trade agreement violation.

Subtitle B: Relief From Injury Caused by Import Competition, Subsidies, Dumping, and Unfair Trade Practices

SECTION 201 (Trade Act of 1974): IMPORT RELIEF UNDER THE "ESCAPE CLAUSE"

o	Transfers decision-making authority from the President to USTR.	o	No position, although opposes transfer under Section 301.
o	Sets up procedures for Industry Adjustment advisory group to prepare industry adjustment plan, which International Trade Commission (ITC) would consider in its deliberations.	o	Opposes adjustment plan concept as unworkable and unrealistic given limited statutory deadlines in Section 201 cases.
o	Requires ITC to estimate the effect of 201 action on domestic competition and on consumer.	o	Supports such consideration.
o	Provides temporary relief for perishable products cases, provisional relief when there are critical circumstances.	o	No position.

o Expedites consideration of Trade Adjustment Assistance (TAA) petitions.	o Opposes TAA as duplicative of other programs.
o Establishes TAA trust fund from revenues of tariffs or auctioned quotas to fund retraining programs under TAA.	o No position on Trust Fund; opposes additional tariffs to fund TAA.

SECTION 406 (Trade Act of 1974): MARKET DISRUPTION (NONMARKET ECONOMY IMPORTS)

o Effectively lowers standards for determining market disruption due to nonmarket economy (NME) imports.	o Supports injury test as sole basis for relief from NME imports.
o Transfers authority for final decisions from the President to USTR.	o No position, although opposes transfer under Section 301.

COUNTERVAILING DUTY AND ANTIDUMPING STATUTES (Tariff Act of 1930)

o Sets up procedures for diversionary dumping cases, when product, subject to U.S. dumping order is dumped in third country, then further processed and exported to the United States.	o No position on legislative proposals. Supports negotiations to cover diversionary dumping under multilateral agreements.
o Special provision for processed agricultural products here looking at relation between unprocessed and related processed imports.	o No position.
o Makes certain strictly domestic financing practices clearly subsidies under countervailing duty law.	o Opposes definition of strictly domestic preferential financing practices as a countervailable subsidy.
o Allows civil suits in Court of International Trade for damages due to dumping.	o No position.

o Prohibits refunding under duty drawback of antidumping/countervailing duties.	o No position.
o Makes natural resource pricing practices subsidies if not available to U.S. firms at same price as to country's domestic firms.	o No position.

SECTION 337 (Tariff Act of 1930): INTELLECTUAL PROPERTY RIGHTS

o Accelerates timetable and expands authority for ITC to act on intellectual property rights.	o Supports shorter time period for determination by ITC on whether to issue temporary exclusion orders.
o Removes requirement to prove injury in intellectual property rights cases.	o Supports use of infringement as sole basis for injury determination.
o Gives USTR final decision-making authority, now with the President.	o No position, opposes transfer under Section 301.

TRADE NEGOTIATIONS

o Extends tariff negotiating authority until January 3, 1989, with provision for three year extension. Maximum 60% unless present duty is 5% or less. Maximum increase of 20%. Any changes for items not on GSP list would have to be approved under "fast track" by Congress. Nontariff barrier negotiating authority has same term extension as tariff authority; but cannot be used until international monetary conference is convened, or President convinces Congress a conference cannot be held.	o Supports extended tariff and nontariff negotiating authority. Opposes any significant restrictions on President's negotiating authority, including linkage to proposed international monetary conference.

o	Five year authority for bilateral talks with Canada on tariff cutting.	o	Supports.
o	Negotiating objectives include: (a) dispute settlement; (b) services; (c) agriculture; (d) natural resources; (e) LDC graduation; (f) intellectual property (g) escape clause procedures (safeguards); (h) tackling problem of countries with consistently large trade surpluses; (i) coordination of international trade and monetary policies; (j) investment; (k) rules on workers rights; (l) countertrade.	o	Support many of these objectives; oppose mandatory negotiations.
o	Provides compensation authority for trade restrictions that violate GATT.	o	No position.

Subtitle E: Miscellaneous Trade Law Provisions

SECTION 232: NATIONAL SECURITY CASES

o	Shortens to three months, with one three month extension, time period for Secretary of Commerce investigation. Also limits time period for President's decision.	o	Opposes.

FAIR TRADE ADVOCATES BRANCH

o	Sets up office in USTR that would in essence serve as lawyer in countervailing duty, antidumping and Section 337 cases for firms that don't have resources to handle case on own or fear foreign repercussions.	o	No position.

TITLE II--INTERNATIONAL TRADE IN TELECOMMUNICATIONS PRODUCTS AND SERVICES

o Requires bilateral negotiations to open up markets of countries USTR determines do not provide U.S. firms equal market access.	o Supports.
o Mandates Presidential market action to guarantee reciprocal access for telecommunications products if negotiations fail.	o Opposes mandatory Presidential retaliation, if no agreement is reached.
o Provides compensation authority if the United States takes action not legal under GATT.	o Supports.

TITLE III--EXPORT ENHANCEMENT

Subtitle A: Export Promotion

o Provides statutory authority for U.S. & Foreign Commercial Service.	o Supports in principle.
o Establishes a Market Development Cooperator Program in the Commerce Department, patterned on Agricultural Department program that is designed to increase exports.	o Supports in principle.
o Reaffirms statement in 1985 Farm Policy calling for strong agricultural trade policy. (Other agricultural provisions incorporated in Title VI.)	o Supports in principle.
o Reaffirms support of Eximbank.	o Supports in principle.

Subtitle B: Export Controls

o Expands statutory conditions on and Congressional review of North slope crude oil exports.	o No position.
o Authorizes use of distribution licenses for multiple exports to the PRC.	o No position. (Supports in principle.)
o Eliminates licensing requirements for reexports of U.S. goods among COCOM countries and for U.S. parts and components, incorporated in foreign-made products, under certain levels.	o No position. (Supports in principle.)
o Eliminates licensing requirements for low technology items (those requiring only notification under COCOM rules) to all free world countries.	o No position. (Supports in principle.)
o Requires the Secretary of Commerce to review portions of the Commodity Control List quarterly, with entire list reviewed annually. Requires the Secretary of Defense to review Militarily Critical Technologies List on an on-going basis.	o No position.
o Requires the Secretary of Commerce, working with the Department of Defense, to suggest to Congress and COCOM removal of items amounting to 40% of the list. Implemented over a three year period.	o No position.
o On foreign availability, expands definition to allow for decontrol on country-by-country basis if country in question has comparable controls. Redefines availability in fact to cover goods not controlled or where controls are ineffective for other countries.	o No position. (Supports in principle.)

o Requires inclusion of industry reps on U.S. delegation to COCOM for purposes of list review.	o No position.
o Prohibits Customs Service from detaining or seizing for more than ten days goods determined by the Secretary of Commerce to be eligible for export under General License.	o No position. (Supports in principle.)
o Authorizes $5 million for the Office of Export Administration at Commerce above requested level.	o No position.
o Requires General Accounting Office (GAO) report on Defense Department review of licenses to non-COCOM countries.	o No position.

Subtitle C: Debt, Development and World Growth

o Requires negotiations on macroeconomic policy coordination and economic growth.	o Opposes mandatory negotiating initiatives.
o Requires Treasury Secretary to issue report on efforts to stabilize exchange rates.	o No position.
o Calls for trade liberalization in LDCs, maintains comparative advantage principles, opposes investment in surplus or injurious commodities.	o Supports.
o Says foreign aid shall be consistent with long-term trade liberalization policies of recipients.	o Supports.
o Overseas Private Investment Corporation (OPIC) reaffirms support for, permits staff increase, authorizes increase in loan guarantee ceiling from $150 to $200 million and increase in direct investment finance from $15 million to $25 million.	o Supports retention of OPIC programs. No position in funding authorization changes.

o Increases World Bank lending resources.	o Supports in principle as part of Program for Sustained Growth, along with economic policy reforms in recipient nations.
o Trade and Development Program, reaffirms support and increases authorization from $20 to $25 million.	o No position. (Supports in principle.)
o Sets up an interagency group, chaired by Commerce, to determine how countertrade might help A.I.D. programs and export opportunities.	o No position.

INTELLECTUAL PROPERTY RIGHTS PROVISIONS

o Makes intellectual property a priority issue, calls for International Development to use funds to train foreign government officials in related enforcement activities.	o Supports. (Sense of Congress language.)

TITLE IV--BANKING COMMITTEE PROVISIONS

o Calls for international conference on monetary reform and exchange rates, and active intervention in foreign currency markets. Establishes strategic currency reserve.	o No position.
o On multilateral development banks, calls for expedited loan activity, upping World Bank shares of projects, more structural adjustment lending by World Bank, changing gearing ratio from 1:1 to 2:1 for World Bank lending, more participation in cofinancing, and tying lending to trade liberalization.	o Supports in principle as part of Program for Sustained Growth (Baker initiative); no position on specifics.
o Capital flight, tying aid to trade liberalization, purchasing oil from major debtors for strategic reserves, study easier writeoffs for loans.	o Supports in principle.

o Expresses support for Multilateral Investment Guarantee Agency, new arm of World Bank to provide investment risk insurance.	o Supports participation in and contribution to MIGA.
o Strengthens existing U.S. mixed credit program by establishing that AID may use Economic Support Funds for mixed credits; provides that the National Advisory Council may approve financing by majority vote.	o Supports.
o Sets up Council on Industrial Competitiveness with reps from government, business, labor and academia to develop strategies for U.S. competitiveness. Will issue report and recommendations within one year. $25 million authorized.	o Opposes Council on Industrial Competitiveness as a form of national industrial policy.

TITLE V--EDUCATION AND TRAINING FOR AMERICAN COMPETITIVENESS

EDUCATION PROVISIONS

o Creates two new grant programs for state agencies and for universities. Programs focused on literacy, vocational education, mathematics education, science and languages. $400 million in funds authorized per year.	o Supports strengthened educational programs. Opposes new federal funding.

TRAINING PROVISIONS

o Three new programs under Job Training Partnership Act (JTPA) and job bank. Would provide grants to agencies helping workers affected by imports, including assistance for training, counselling, relocation. Eligibility based on industry, not specific firm injury. Also gives grants to labor-management committees on retraining and has pilot retraining voucher program.	o Opposes new JTPA programs as duplicative of existing programs. No position on voucher program.

TITLE VI--AGRICULTURAL TRADE

o Calls for organization of Agricultural Department with respect to trade policy for farm products.	o Supports.
o Calls for long-term trade strategy reports at regular intervals.	o Supports.
o Requires report on relation of food aid to market development, plus sets up new Food Aid Policy office.	o Supports.

TITLE VII--FOREIGN CORRUPT PRACTICES, ADJUSTMENT PLAN REVIEW AND TEXTILE IMPORT ADJUSTMENTS

FOREIGN CORRUPT PRACTICES PROVISIONS

o Establishes new culpability standard, eliminating "reason to know" standard and replacing it with whether executive has behaved in reckless fashion or has knowledge of bribe.	o Supports in principle.
o Defines permissible "grease payments" as those made to obtain "routine" service or are legal in host country.	o Supports.

ADJUSTMENT PLAN REVIEW

o Sets up review committee, chaired by the Commerce Secretary and consisting of USTR, Labor and Treasury Secretaries, to oversee implementation of adjustment plans in conjunction with Section 201 relief and make recommendations to USTR that relief end if it looks like plans aren't being followed.	o Opposes review plan as step toward national industrial policy.

TITLE VIII--TARIFF AND CUSTOMS PROVISIONS

o Includes over 60 miscellaneous duty bills (suspensions, reclassifications), implements Nairobi Protocol on cultural materials.	o No position.

OTHER AMENDMENTS ADOPTED ON HOUSE FLOOR

- New U.S.-Mexico Commission for bilateral economic relations, by Representative Ronald Coleman (D-Texas) as amendment to Title III.
- Japanese Semiconductor Policies, call for Japan to open markets and for President to make determination in Section 301 case, by Representative Les AuCoin (D-Oregon), as amendment to Title I.
- Requirements for the Administration to issue new regulations speeding up negotiations on new limits on textile products, within 90 days, by Representative James Broyhill (R-NC), as amendment to Title VII.

International Division
U.S. Chamber of Commerce
February 18, 1987

Chamber of Commerce
of the
United States of America

January 16, 1987

Edward Donley
Chairman of the Board

1615 H Street, N.W.
Washington, D.C. 20062
202/659-6000

The President
The White House
Washington, D.C. 20500

Dear Mr. President:

On September 5, 1985, my predecessor, Frank Morsani, wrote you concerning the importance of public support for an open world trading system and action on your part to maintain that support. He particularly urged you to take a much tougher stand against foreign unfair trade practices through aggressive use of Section 301 of the Trade Act of 1974 and other existing trade remedies. We were pleased to note that you did indeed commence several such actions in the following weeks and months. Those actions have helped alleviate domestic pressure for more drastic, and less prudent, policy actions. Moreover, an aggressive U.S. stance against unfair practices is needed to preserve public confidence in U.S. trade law and a liberal trading system.

Unfortunately, however, our trade position continues to deteriorate despite actions taken thus far. Even though foreign unfair trade practices are responsible for a relatively small share of our trade deficit, their persistence reflects a belief among our trading partners that the United States is reluctant to do what needs to be done to protect its legitimate interests in a fair and open trading system. Furthermore, many of our members, including some of our most successful exporters, complain that other countries exclude U.S. access to their markets knowingly and in violation of international and bilateral agreements, but with little fear of adverse U.S. government action. It is for this reason that the Chamber has favored mandatory retaliation against such practices when they violate international trade agreements.

There is no doubt in our minds that the 100th Congress will pass trade legislation. We think there is great potential for constructive change in this regard, and we intend to continue working closely with the Congress. We are encouraged by your administration's expressed willingness to do likewise. It is our hope that we can work closely with you and the Congress to enact trade legislation that is not protectionist, will address effectively unfair trade practices of our trading partners, will eliminate the self-imposed disincentives to American exports and will consider the broader, more fundamental competitive issues.

While we are continually assessing proposed trade law changes, it is clear to us, for example, that continued violations of U.S. intellectual property rights abroad require a decisive response. Violations of U.S. intellectual property rights constitute a significant threat to U.S. international competitiveness and foreign trade performance. We appreciate your long-standing support for strengthened protection in this area. To bolster business community efforts to secure effective intellectual property protection, the U.S. Chamber is creating an Action Center on intellectual property which will gather comprehensive information on this subject and make action recommendations to both the U.S. and foreign governments for eliminating violations of U.S. intellectual property rights.

We also believe that U.S. law includes far too many unwarranted, self-imposed disincentives to U.S. exports. United States antitrust laws need to be examined to ensure that they do not undermine U.S. competitiveness, domestically and overseas. The U.S. Chamber strongly opposes bribery and supports the objectives of the Foreign Corrupt Practices Act. However, that Act, as currently written, is sufficiently vague so as to effectively discourage U.S. companies from pursuing foreign business in ways that were not intended to be prohibited. In addition, there is an urgent need to revamp export control statutes and regulations to eliminate unnecessary controls on U.S. exports which not only fail to improve national security, but also severely undermine the legitimate commercial interests of the United States, not only in terms of sales, but also in technological innovation.

There is also a good deal of concern that Section 301 itself, as potent a statute as it is, does not provide for sufficiently certain recourse against foreign unfair trade practices. For this reason, the U.S. Chamber is currently surveying those companies and other organizations that have filed Section 301 petitions since 1975 to determine whether that law, as currently written, provides effective recourse against those practices. We hope to reach some conclusions and develop some recommendations in the near future.

Foreign unfair trade practices cost U.S. businesses billions in lost market opportunities every year. More importantly, they deflect attention from other problems which contribute much more significantly to our trade imbalance. The issue of America's ability to compete in the world marketplace is justifiably at the top of the national agenda. America's global position requires the highest priority and attention. No one is more convinced than the U.S. Chamber of our ability to harness our creative ingenuity, management expertise and extensive pool of human resources to enhance U.S. competitiveness at home and abroad. To do this effectively, government leaders must cooperate in promoting policies which sustain an environment conducive to economic growth and global competitiveness.

In conclusion, we applaud your efforts in the past to address this issue in a positive way. But much more needs to be done. We urge you to work with the Congress in developing constructive trade legislation. We encourage you to pursue actions at the executive level which will move us toward our common goal of strengthened U.S. competitiveness and an open, expanded world trading system. We wish you well and stand ready to assist you in any way that we can.

Sincerely,

Edward Donley

Edward Donley

PREPARED STATEMENT OF RICHARD BAROVICK, EXECUTIVE DIRECTOR, NATIONAL FEDERATION OF EXPORT ASSOCIATIONS

Good morning, my name is Richard Barovick, and I am Executive Director of the National Federation of Export Associations. Our Federation was created in 1984 to provide a voice in Washington for the nation's export management company industry, and is now being expanded to include other exporter associations.

The Federation's current roster of member groups comprises NEXCO (based in New York), the Export Managers Association of California (based in Los Angeles), and the Overseas Sales Marketing Association (based in Chicago). In addition, the Overseas Automotive Club (based in New York-New Jersey, but with a nationwide membership) has joined as an associate member.

The U.S. export management company industry comprises about 1,000 firms nationwide that serve as the export representatives or departments of manufacturers of all sizes and products. With each of our exporters handling an average of ten manufacturers, we represent approximately 10,000 American producers as an industry.

The export management companies are a natural answer to the needs of smaller manufacturers that make exportable products but lack the know-how, international marketing networks, and finances to build overseas markets on their own. We are an industry of smaller firms that tends to serve smaller firms in international sales. However, because our member-companies specialize in certain product sectors and in certain geographic areas, they often are able to market the products of large manufacturers as well. One member-company, for example, specializes in the export of food products and food-processing machinery, and has a well-established niche in Asian and Middle Eastern markets. It, therefore, currently serves as the export arm of several quite sizable U.S. food processing firms in certain key markets. Another member-company is building Asia-Pacific markets for U.S. manufacturers, large and small, of educational equipment.

In recent years, our industry has been beleaguered by the same external factors that have dampened American exporters across the board. The high value of the dollar and the Third World debt burden have made exporting very difficult. For smaller exporters, such as export management companies, these external factors have had an exaggerated impact that has produced some thinning in the ranks.

Now, however, our members find a new opportunity to build export markets: the falling value of the dollar has made American prices competitive once again, and the quality of many American products has improved, as companies have tried harder to meet the global marketplace. The most pressing remaining problem — and we face several — is a lack of export finance. The U.S. banks have, to an alarming extent, dropped out of export credit operations and that has cramped the ability of many export management companies to get back into overseas business.

I would like to make two general points on the problems facing our industry and then focus on a menu of suggestions for Congressional action. We are especially grateful for the opportunity to testify before the House Small Business Committee because it is uniquely focused to take our industry and our problems seriously.

The first point I would make is that the Washington dialogue over exporting tends to concentrate on the policy arena rather than on exploring the kinds of programs that would help a small industry such as our own. Most of the talk is about either foreign relations or the governmental regulation of business. Topics such as keeping our high-tech products out of the hands of the Soviet Union; quarrelling with Japan, Korea, Taiwan, and Brazil over restricting our access to their markets, and negotiating over a new set of international trade rules are what command the attention of policy makers. The notable exception is the dialogue over the U.S. Export-Import Bank, where effective communication, mostly by larger companies, has produced a sensible discussion and a valuable institution.

The second point I would like to make is that our industry has a recognition problem, and it is a problem that surfaces in various ways. Let me offer some examples. One is that we do not have an SIC number for trading companies, so that no one has precise data on how many there are. This is an unfortunate informational gap. The Commerce Department included an article on our industry in its "U.S. Industrial Outlook" in 1987 for the first time, and that was a real help, since it acknowledges in an official way that we exist. But even that article referred to the absence of an SIC number.

Another example is a report in "The Washington Post" on February 8 that cited the comments of Sam Beard, chairman of the National Commission on Jobs and Small Business on the problems facing small business exports. Mr. Beard is reported to have said that it is difficult for many small companies to cultivate foreign business. He remarked: "There's no mechanism either in the private sector or the public sector combined to stimulate that." Apparently, after several years of staff work, numerous meetings, and, I am sure, countless speeches, Mr. Beard apparently has not heard of the export management company industry and its role in building small business exports. Now that our Federation has its letterhead printed, I can send Mr. Beard a letter.

This is a real problem, since smaller manufacturers should be aware that they have a choice in developing a strategy for exports. Either they can pursue them on their own, or they can use the services of an export management company. They should know that such a choice is available, and it ought to be one of the functions of government -- at federal, state, and local levels -- to educate small business on the resources available to them. The federal government makes little effort to do so at this time.

A third, and final, example of this recognition problem arose in 1982 when Washington got interested in exporting trading company legislation. Here I am reminded of a speech I heard many years ago by Carlos Romulo, at that time the Philippine government's Secretary of Foreign Relations. Mr. Romulo said, as I recall: "In 1519 Magellan sailed across the Pacific and discovered the Philippines...and there we were." What happened in 1982 was that the discovery of trading companies managed to overlook our export management company industry and instead a law was passed that empowered banks to enter the field, setting up trading company affiliates, and changes in the antitrust laws were adopted to provide more protection where companies team up in exporting. It never explored what might be helpful for our kind of trading firms.

This year, Congress is considering amending the 1982 Export Trading Company Act, and may in the process forget the original purpose of the 1982 statute. The key issue is what constitutes a bank trading company. The 1982 law stressed that such firms should be primarily engaged in exporting though they may also pursue imports and third-country transactions. The Federal Reserve, in its regulation of bank ETCs, requires the banks to generate 51 percent of their trading income in exports, and to reach that calculation within two years. Now, the Administration and others want to water that down, and count third-country transactions as part of the export figures. That would mean that several larger banks could simply focus their efforts on third-country transactions abroad, never export any American products, and count those overseas dealings as a U.S. service export. It could be easy to arrange some slight U.S. bank involvement, to make it count as an American export -- not of goods, but of services. This could distort the whole public purpose of the 1982 law.

Though the banks have complained about the Federal Reserve's rules, apparently if a bank wants to export U.S. goods it can do so quite nicely under the present regulatory framework. First Interstate Bank in California reports that it exported $40 million worth of goods in 1986 and will do at least $60 million in 1987, and all that despite the Federal Reserve rules.

On the brighter side of the 1982 Act, a few banks have actually used their ETCs to finance trade, which is a good role for banks, the kind of activity that they know well. In that role they can help the export of American goods, including those sold by export management companies.

On the antitrust side of the 1982 law, by coincidence, the 1984 Shipping Act combined with the ETC Act has made it possible for exporters to join together in forming shippers associations. Through this device they can negotiate more favorable freight rates with ocean shipping lines. NEXCO, the New York-based export management company group that is part of our Federation, has creatively responded to this opportunity, creating the NEXCO Shippers Association. Membership in the shippers group is growing rapidly, and includes both small and large exporters.

The House of Representatives is in the closing days of work on two key pieces of trade legislation. One is the omnibus trade bill, which I was delighted to find will have a small business title. The other is the effort to revise the 1982 Export Trading Company Act, which may be considered either as part of the omnibus bill or on its own. So there are opportunities to adopt legislation that might address the problems and the contributions of our industry.

I would like to suggest a few items for your consideration in writing these laws.

1. Awareness. It would help the nation's smaller manufacturers of exportable products to recognize that a resource to pursue foreign markets is available in the export management company industry. This can be achieved by having such federal institutions as the Small Business Administration and the Commerce Department promote that awareness in cooperation with state and local governments. Wherever SBA, Commerce, and the states approach small or new exporters, they can educate them on the availability of that choice.

Filling in the data gaps would be quite helpful, through creation of an SIC number for trading companies, and through development of surveys that could draw a portrait of the export management company and other trading company resources across the country. In pursuing this information we would be in a position to identify how best to link manufacturers and exporters.

2. Networking. Beyond simply promoting awareness of the export management company concept, it would be helpful to develop a nationwide networking program, perhaps started on a pilot project basis, that would aim at systematically introducing manufacturers and exporters.

3. Export finance. The National Foreign Trade Council, a New York-based industry group, did a study of bank involvement in foreign trade and concluded that the U.S. commercial banks have seriously withdrawn from the field. The U.S. Export-Import Bank has drawn the same conclusion. Our export management companies are especially hard hit by this situation, since they have less access to bank credit than the major exporters. Banks are reluctant to handle smaller transactions, which are the typical ones for export management companies. And banks are reluctant to take country risks these days.

Fortunately, the U.S. Eximbank is attempting to fill this gap and to bring the banks back in. And the Eximbank has created an association program that is just getting underway. No sooner did I send out the press release announcing my new activity with the Federation than I received a letter from the Eximbank inviting us to come in and explore ways to make this association program work for our Federation.

What is more, the new Eximbank strategy is to permit any responsible party to come in and borrow and then lend to foreign buyers. So perhaps export trading companies, including export management companies, may be in a new position where they can obtain the funds and become lenders. This is a brand-new situation, and we have to explore how to make it work for us. It is an area worth watching.

4. Apprenticeship. One of the heavy costs for export management companies is the start-up expense of taking on a new manufacturer client. The investment in building that manufacturer's export marketing network is sizable. We think it would be helpful for government to consider creation of an apprencticeship program that would provide an intern for a year, perhaps a graduate student or a recent graduate, who could work on the new export effort. The apprentice could receive a formal certificate, and the nation would benefit from having a newly-trained professional exporter. The government's investment could be paid back out of the earnings of the new export stream of activity.

5. Trade fairs abroad. Participation in trade fairs abroad can be a valuable part of overseas marketing. Many foreign governments help pay for the participation of their exporters, and some provide a tax incentive for such trade fair marketing. We can provide some examples of how this is being done abroad. In Massachusetts, the port authority called Massport does something comparable. It covers part of the expense of a small business exporter engaged in marketing operations abroad. We would like to see a U.S. program along these lines created. We think that U.S. and state governments can provide funds (which can be recaptured through sales and earnings) and offer tax incentives for the exporter's own spending.

6. Cooperator office. The House Foreign Affairs Committee's Subcommittee on International Economic Policy and Trade has just adopted the concept of a Commerce Department export cooperator program for manufacturers, based on the model long established in the Agriculture Department for commodities exporters. Expenses would be shared between private industry and the Department. We think this excellent idea should be aimed at export management companies, so that an office could be opened for EMCs in a key market such as Japan, Korea, Taiwan, or Brazil.

Our Federation is in a new, expanding phase, and I have just assumed my new role as Executive Director. Therefore, we are still trying to develop an agenda, and will report back to you further. These are just some of the ideas that have been considered in our group. We would welcome an opportunity to work with your committee in the months ahead in devising fresh solutions to our industry's challenges. We view ourselves as a multiplier sector. Our own Federation has about 500 export management companies in its ranks so far, including the four associations. If each exporter handles ten manufacturers and if each producer exports as little as $500,000 per year each, that means we are addressing a total of $2.5 billion. If we can stimulate another $500,000 each, we would achieve a $5 billion export business. That is enough to deserve the attention and support of the federal government.

PREPARED STATEMENT OF MICHAEL CAMPBELL, PRESIDENT, NOVA TECHNOLOGY CORP., AND CHAIRMAN, SMALLER BUSINESS ASSOCIATION OF NEW ENGLAND, INC., REPRESENTING NATIONAL SMALL BUSINESS UNITED

Mr. Chairman, and members of the Committee on Small Business, it is indeed a pleasure to have the opportunity to testify on some of the major issues that affect small business in the coming months and years. Competition is a familiar word to small business and one that we thrive on. In the USA most small businesses have to survive in a highly competitive environment, whether it be competing for new markets, products, competent personnel to run the company or even for capital to finance the firm. Extended work hours go with the job and it is not unusual for the entrepreneur to regularly work six and seven day weeks. Indeed, it is this spirit of commitment to do the best job possible, that permeates our society, and distinguishes our people, government and industry as a model for the rest of the world to follow. This can be best reflected by the rest of the world's confidence in our abilities as shown by the huge investments from overseas, which have greatly influenced the recent surge in the U.S. financial markets.

But what has happened in recent years? Why does the U.S. not always enjoy the competitive edge in world markets? Why are some people losing their jobs to overseas manufacturers? Why did our trade deficit not rebound from a sharp increase in export sales activity like it was supposed to once the dollar was forced to lower levels against the hard currencies on the world market?

How can some of these problems be faced and overcome without retaliatory actions that could result in protectionist tariffs, like Smoot-Hawley, and ultimately the disastrous economic and unemployment conditions of the 1930's? And how can government help the American small business reignite their competitiveness on the world-wide markets once again?

Although the problems may be severe, they are not insurmountable. For years the United States was a world leader by virtue of its natural resources and in our ability to feed our population far better, and for much less than most of the other countries in the world. When the US competed in the world markets, we did so on a grand scale, through big industry and big agriculture. But aside from this, the first priority was almost always satisfying the needs of the home market which grew from a population of 160 million just after World War II to 239 million today. Nowhere else in the world did there exist such a consumer driven market with money to spend. By contrast, other nations had to always be intensely involved in international trade at all levels of business, to both survive and grow. The size of the U.S. market and disposable income levels of the population was not lost on them, and when the time came to fill the need, they often did so with equivalent or better products, at more compatitive prices. Somehow, with the exception of the multi-national companies that were long established in international markets, and those smaller companies with very unique product lines, exporting products would be put on the back burner in favor of satisfying the local domestic markets first. Then, if we had time, we'd get to the export markets later on.

This attitude must now change if we are going to turn this trade deficit around, and our industry is going to compete on world markets both now and in the future. What has happened to the USA is that today we now find ourselves in the same position as other countries who had to look outside their borders for new markets. We are now an island nation (though, indeed a very big one) that must utilize our spirit of competition and commitment to succeed beyond our borders. And this must and can be done by industry at all levels, but particularly with small business.

What is needed today are simple, workable solutions, that will act as a direct catalyst to prime the pump, and promote international trade in the form of export sales and create new jobs.

What is not needed today, is grandiose legislation that, once enacted, is difficult to understand, cumbersome to implement, and in the end, dies on the shelf for these same reasons.

Accordingly, as I see it, the bottom line answer to the problem lies in three areas: education, incentives and government cooperation.

Education - The Problem: There is a need for trained, qualified staff at an administrative level to get the export paperwork done correctly, and get the shipments out the door. The need is not for the high-powered sales executive, but for the functional "factotum" to get the work done, and at an affordable price to the small company.

The major problem that small business faces, and which distinguishes it most from big business, is lack of resources. This problem is manifested by the inability of the company to be able to afford to hire most qualified people to do the necessary jobs. And in small business the one area that always seems to suffer is the international department, because the qualifying skills are more unique, and the needs are not perceived to be as great as the employment needs to meet the demands of domestic sales.

Many times when an overseas inquiry is received it will be handled by a senior member of the corporate staff who is not really cognizant of export procedures, and as such there is often a fear of the unknown or of looking foolish to other more junior people, if they don't know the correct procedures. These prejudices can be further enforced once they take the second step, and start to get involved with the documentation procedures, and evaluating the different financial alternatives. The ultimate result can be lost orders and opportunities, through an inability to understand and deal with the problem.

The Solution: Small business needs to have more technically qualified people made available to do the international paperwork. There already exists an excellent network of regional and community colleges that can provide these resources at the associate degree level, which will give the average small business a competently trained international trade person, at a most affordable price. Accordingly, new programs in international trade in these schools are to be enthusiastically encouraged.

Incentives - The Problem: One can create wonderful solutions and new legislation to solve the problems, but, if at the end of the day, there are no immediate financial benefits to the small firm, it is probably unlikely that they are going to give such legislation more than lukewarm support.

Indeed, if any new trade legislation is to go far on a positive basis (i.e. the stimulation of U.S. exports) versus a negative basis (i.e. protective tariffs) there has to be a financial incentive to the average small businessperson that is at the same time understandable, attractive, and doable in the general course of business without adding alot of extra paperwork.

The best way to attack the international trade deficit problem is to attack it with a renewed, more aggressive export sales activity from firms of all sizes, with the in-company enthusiasm and commitment that most firms take on when they set out to conquer new markets.

Incentives - The Answer: It is my recommendation that our legislators consider the implementation of a new Export Tax

Credit. This would be a flat 10% tax credit similar to the Investment Tax Credit that was recently phased out in the new tax legislation. Although the ITC was directed to tangible property, the ETC would be a direct offset against the corporate tax bill for any and all costs incurred with international sales. The credit would be applicable to companies with gross sales up to $25 million, and a company could receive the credit for all phases of startup, training and implementation of their international export sales activity at their company. The credit could also be taken by companies whose employees had become redundant due to foreign competition, in retraining them in skills that are more competitive in today's markets.

Government Cooperation - The Problem: With the budget cuts in recent years, small business has been hurt by the reduction and pulling back of activities performed by the Department of Commerce. Of all the immediately available resources to the small businessperson, DOC gives the best, most comprehensive service to the small firm at a price that is affordable. The department similarly has a cadre of well trained, well informed personnel who seem to go out of their way to help companies get started in doing business overseas. Similarly, in the overseas consulates there are local U.S. trade representatives who are highly knowledgable and helpful to the American businessperson passing through. I can personally attest to several instances in Zurich, Frankfurt and London where the efforts of the local trade representative on my own behalf during such a visit, led to a profitable deal being made.

The extent that these functions have had to be reduced or cut back by the budget cuts has severely impacted the small business in trying to find out and understand what it takes to get started in international trade. Furthermore, the cutbacks also represent a reduction in promotional activities that DOC performs, which is sometimes the only mechanism the smaller firm has in showing its products and services to foreign markets.

Then there is also the matter of licensing hi-tech products that contain certain components that may be restricted for overseas sales. This effort can be time consuming, frustrating, and costly when the end a loss of an order to the US Company, because of excessive delays brought about by the license approval process, or even the final inability to deliver the product if the approval is rejected. Again, the lack of resources of the small business in not having qualified people available who are also knowledgable in government's ways can prove detrimental, and lose business for the company. On an extrapolated basis this ultimately affects export sales and American jobs.

Government Cooperation - The Solution: In order to make small business more successful in international markets, the Department of Commerce's International Trade Division's promotional activities must be restored. This includes having available simple, easy to understand, brochures which at least tell the small firms of the DOC resources that are available to them.

Second, the approval process for the export licensing of restricted components could be streamlined to make the process more expeditious. I cannot recommend how this procedure could be done within the department, only that it would certainly help international trade to have it done.

Third, given the overall climate to stimulate export trade and offset the trade deficit, government should look toward providing an incentive to small firms that would get their immediate attention into looking into export sales as a means to expand their markets. Such a mechanism would be the creation of an Export Tax Credit or similar device, as discussed previously.

Finally, to address the four matters of particular concern to this committee, I shall respond as follows:

1] Existing Export Enhancement:

a. Existing export programs provided by DOC should be expanded as often DOC International Trade activities are the small firm's first and only contact with an international trade professional. Money spent on promotion will result increased sales overseas, and ultimately return to the government through increased corporate tax revenue.

b. There is a market gap for financing small orders that particularly impacts small business. As most of the international banking activity is conducted by the large multinational bankers, they are generally not interested in small business until the deals get up into the million dollar range. Indeed, I was personally told by a Boston bank that before they would consider doing any letter of credit activity for my company, I had to set up an international account with a minimum balance at all times of $10,000 in their bank, regardless of our export sales activity for the month.

We need to create a mechanism to underwrite or guarantee funds for smaller export orders.

c. I am not aware that the Export Trading Company initiative has had the success that it was purported to have at the outset of the program. There is definitely a place for the Export Trading Company. But some small companies (particularly Hi-Tech firms) may be better served by having the availability of their own sales force and international organization to compete in foreign markets.

d. The licensing system for smaller, hi-tech firms can prove to be cumbersome and still needs to be streamlined. (See above discussion).

2] Problems in Confronting Increased Import Competition:

I believe that the government should take strong measures against countries that undertake any "dumping" activities to secure a large market by selling at artificially low prices to drive out U.S. competition.

Some products that are highly labor intensive will never be competitively made again in the USA due to our labor costs. Indeed, even Japan is experiencing such pressures today from Korea and Taiwan. In the same way that the skills for making buggy whips became redundant when the automobile was created, so will today's skills similarly be affected in time.

American workers must always have the opportunity to be gainfully employed in productive, growing occupations. In order to ensure jobs, government should create tax incentives that corporations can use to retrain these loyal workers to a. make new products for existing markets, b. create new jobs skills to take companies into new product markets, or c. create new skills to work in complimentary markets.

3. Capital Formation:

In terms of venture capital, there appears to be an ongoing high interest level in funding new ventures. In a recent $80 million public offering for a new such venture group, the offer was totally subscribed within 4 hours after its opening on the exchange.

Growth companies always have a high need for working capital. Programs that make it easier for companies to obtain such working capital more easily from investors (in terms of tax advantages) or from banks (in terms of loan guarantees) are always needed and always welcome. The one request is to try to keep the paperwork as simple and straightforward as possiible.

As a general rule, the lower the capital gains tax, the better it is for improving the market for capital formation and availability for new ventures and growth companies.

Once again, on behalf of SBANE and the small business community, I appreciate the opportunity to appear before this committee today. I shall be pleased to respond to any questions either today, or on a follow up basis by telephone (617)281-1222. Thank you.

NOVA™
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BIOGRAPHICAL SUMMARY OF MICHAEL CAMPBELL

Michael Campbell graduated from the University of New Hampshire with a Bachelor of Science degree in Chemistry in 1968. In 1976 he enrolled at the Massachusetts Institute of Technology where he received his Master of Science degree in Management, with special concentration in international finance.

Early in his career Mr. Campbell served as an operations officer with British Overseas Airways and also on the international marketing staff of Goodyear International Corporation. He then moved to Cabot Corp. in Boston, Massachusetts where he served as an international marketing officer. Subsequently, he was offered and accepted a position as Manager of Commercial Development for the Nashua Corporation in Nashua, New Hampshire where he was responsible for all new markets and new business of the company. In 1976 Mr. Campbell formed NOVA & Company; a consulting firm specializing in international trade issues for small business. In addition to small business, Mr. Campbell has also acted as a contract consultant to Arthur D. Little, Inc. of Cambridge, Mass.

In 1982 Mr. Campbell founded NOVA Technology Corporation of Gloucester, Massachusetts a high technology, electronics manufacturing company, and has served as its President and CEO. Mr. Campbell is a member of the Board of Directors of the Smaller Business Association of New England and serves as the Chairman of its International Trade Committee. He is also active in the New England Fisheries Institute, and serves as Chairman of the UNH North Shore Alumni Association and the American chapter of the Old Stortfordians Society.

Statement of the Chamber of Commerce of the United States

ON: U.S. SMALL BUSINESS AND INTERNATIONAL COMPETITIVENESS

TO: HOUSE COMMITTEE ON SMALL BUSINESS

BY: EDWARD DONLEY

DATE: MARCH 24, 1987

The Chamber's mission is to advance human progress through an economic
political and social system based on individual freedom
incentive, initiative, opportunity and responsibility

The U.S. Chamber of Commerce is the world's largest federation of business companies and associations and is the principal spokesman for the American business community. It represents approximately 180,000 businesses and organizations, such as local/state chambers of commerce and trade/professional associations.

More than 91 percent of the Chamber's members are small business firms with fewer than 100 employees, 58 percent with fewer than 10 employees. Yet, virtually all of the nation's largest companies are also active members. We are particularly cognizant of the problems of smaller businesses, as well as issues facing the business community at large.

Besides representing a cross section of the American business community in terms of number of employees, the Chamber represents a wide management spectrum by type of business and location. Each major classification of American business--manufacturing, retailing, services, construction, wholesaling, and finance--numbers more than 11,000 members. Yet no one group constitutes as much as 29 percent of the total membership. Further, the Chamber has substantial membership in all 50 states.

The Chamber's international reach is substantial as well. It believes that global interdependence provides an opportunity, not a threat. In addition to the 56 American Chambers of Commerce Abroad, an increasing number of members are engaged in the export and import of both goods and services and have ongoing investment activities. The Chamber favors strengthened international competitiveness and opposes artificial U.S. and foreign barriers to international business.

Positions on national issues are developed by a cross section of its members serving on committees, subcommittees and task forces. Currently, some 1,800 business people participate in this process.

I. INTRODUCTION: SETTING THE SMALL BUSINESS POLICY AGENDA

Mr. Chairman and members of the Committee, I am Edward Donley, Chairman of the Board of the U.S. Chamber of Commerce. It is a privilege to appear before you today to discuss small business and international competitiveness. Accompanying me today is Thomas E. Donley, the Director of the Chamber's Small Business Center.

The U.S. has been blessed with many resources, which have propelled us from being a backwards colony to the preeminent nation in the world in just 200 years.

But, other nations without our resources have learned to become skilled in international trade out of economic necessity. These nations, more so than the U.S., apply international competitiveness as the crucial test in adopting policies that affect their businesses.

The ability of U.S. businesses to compete successfully in international markets is more important today and more in question than at any other time in our history. I commend Chairman LaFalce for holding these hearings as part of a nationwide consciousness-raising in which we have been engaged for several years. I am confident that as a nation we will make the necessary adjustments now that the American people have set their sights on the competitiveness problem. But the hard work is just beginning, with each worker needing to develop his or her skills to be productive, each company managing resources carefully while improving the quality of products, and each school demanding excellence in the classroom. And here in Washington, Congress and the Executive Branch must work on streamlining and retooling the federal government, educating the electorate about the limits of the federal government and relying more on state and local government for desired public services and on the private sector for jobs, productivity and income.

On December 1, 1986, I retired as Chairman and Chief Executive Officer of Air Products and Chemicals, Inc., headquartered in Allentown, Pennsylvania. I am currently Chairman of the Executive Committee of the Board of Directors. I began working at Air Products as a draftsman, part-time while I was in college, and joined the company full-time in 1943. Today, Air Products is one of the 250 largest industrial firms in the U.S., employing more than 18,000 people and doing business in 18 countries. However, when I joined the company, I was the eleventh employee, in a small start-up company. I am proud to be part of an American success story, a company that has grown from being an entrepreneurial start-up bankrolled by the founder's father-in-law to a publicly held international corporation, which relies as much as ever on entrepreneurial marketing and technological innovations to be able to compete in world markets.

The spirit of entrepreneurship that has motivated Air Products' growth along with so many other small businesses in the U.S. is alive and well, but it requires a hospitable monetary, regulatory, tax, and trade climate in which to prosper. Last August, the 1986 White House Conference on Small Business (WHCSB) adopted a short-term legislative agenda to produce this climate. And the National Commission on Jobs and Small Business (National Commission), in its report released last month, created as good a long-term agenda as I have seen. Members and staff of the Chamber were involved actively in both of these events. We take pride in the striking similarities between those short-term and long-term recommendations and the Chamber's policies. For more than a year, the Chamber's theme has been "Let's Sharpen America's Competitive Edge," a theme that reflects the recognition of the need for American business, labor, and government to adapt to a shifting environment and changing business priorities, particularly ones that will allow our small business sector to grow.

We appreciate the interest that members of the House Committee on Small Business have taken in the WHCSB and in the National Commission, particularly Chairman LaFalce and Representative McDade as congressional conveners of the National Commission, and Representative Ireland, for spending so much of his personal time at the WHCSB.

It is important that as we concern ourselves about competitiveness, we do not draw a gloomy conclusion about our economic future. In 1986, inflation in the U.S. had its smallest increase in two decades. Interest rates, although high by historic standards, are the lowest in a decade. In February of 1987, civilian employment hit a new peak of 111,382,000, an increase of over 11.0 million people at work since January 1981, with 62.0 percent of the adult population working--the greatest proportion in our nation's history. Industrial production has increased by over 26 percent since the end of the recession in 1982, and productivity per hour has increased by six percent. The U.S. is the world's largest exporter, in addition to being the world's largest importer; and contrary to public perception, our share of world production has remained the same not decreased. In 1980, the U.S. produced 28.5 percent of total world products, and in 1985 the U.S. produced the same percentage.

Rather than exult that national policies have made the U.S. economy the envy of the world or despair that the only solution to our trade deficit is to close our markets to foreign businesses, we must take the next steps to implement our free enterprise philosophy by encouraging other nations to adopt pro-growth, free enterprise policies, and thus help ourselves as well.

At the same time, the U.S. needs to take the tough actions necessary to get a level international "playing field," and to improve programs that will foster increased exports. We must not let the budget deficit reduction imperative cause us to cut into programs that help to keep our goods competitive in world markets. If we have any faith at all in cutting the budget deficit through economic growth, we must not sacrifice our export industries in the budget-balancing process.

The Chamber believes that in order to make our businesses more competitive we must first remove domestic disincentives to business performance and also pursue the following objectives in international trade:

- o Develop and support policies and programs to increase exports;
- o Press for the elimination of foreign tariff and non-tariff barriers to U.S. trade and investment; and
- o Improve the ability of U.S. firms to compete domestically by providing effective domestic recourse to foreign unfair trade practices and injurious imports, while ensuring U.S. consumers access to fairly traded goods and services.

I would like to comment on the U.S. Chamber's recommendations regarding these four objectives.

II. REMOVE DOMESTIC DISINCENTIVES TO BUSINESS PERFORMANCE

The Chamber is concerned that Congress may enact legislation that is contrary to the recommendations of the WHCSB and the National Commission. These small business initiatives seek to preserve a business owner's right to manage, reduce the government's regulatory burden on the business community, maintain incentives for capital formation, and maintain a healthy, predictable business environment.

The Chamber urges the Committee to take the lead in Congress in opposing legislative initiatives that would adversely impact these recommendations and reverse the broad-based policy reforms begun in the Carter Administration and accelerated in the Reagan Administration. Such legislation as parental leave, anti-dual shop, mandatory health insurance, increasing the minimum wage, and plant closing and the lack of a national product liability bill are or could be impediments to businesses' operating in the most efficient manner possible.

If small businesses are to continue growing as they have in the past decade, Congress and the government as a whole must respond to their special needs.

The first, is a federal product liability bill. As the Committee knows, liability insurance is crucial for any business operation. The prohibitive costs or unavailability of liability insurance, especially in the product liability area, present obstacles for the small business owner who wishes to remain competitive.

The number one recommendation of the WHCSB called for relief from the "liability crisis," including the establishment of federal product liability standards. The Chamber urges the Committee to review carefully the recommendations of the WHCSB in this area. We look forward to working with Congress to pass product liability legislation that will eliminate joint and several liability, cap noneconomic damages, return to a fault-based standard of liability, and limit contingency fees to reasonable amounts on a sliding scale.

I would like to add several thoughts on capital formation and technology transfer. In capital formation, again, broad-based solutions, allowing capital to achieve the highest return, will be of the most help to small businesses. Reducing the capital gains rate in 1978 and again in 1981 encouraged people to save, and to invest in venture capital, which grew from about $500 million per year in 1975, to $13 billion per year in 1983. This is "patient capital," carrying high risk but offering high returns, the kind that small businesses desperately need. Ending the capital gains deduction in the 1986 Tax Reform Act is one of the most damaging actions that the federal government could have taken with regard to economic growth.

The Chamber believes that lower marginal rates and incentives to invest in capital are both important features in the tax code. The Investment Tax Credit and the Accelerated Cost Recovery System were very valuable to small business. Some liberalization of capital cost recovery allowance is necessary to promote small business investment. We urge this Committee to take the lead in Congress to restore the capital gains differential on behalf of small businesses, and to retain the low marginal tax rules that will be fully phased-in in 1988.

In addition, the federal regulations that limit interstate banking and prevent most banks, particularly smaller banks, from making equity investments in small businesses need to be amended. These outdated restrictions contribute to the short-term lending orientation of banks. The financial distribution system in the U.S. is the best in the world, including 14,000 banks, with at least one and usually several, competing for business in almost every city and town across the country. If Congress would allow banks to make limited equity investments in small businesses, we no longer would hear the complaints that venture capital is limited only to major financial centers in the U.S.

Also, public and private pension policies and practices need to be studied to determine what can to be done to increase pension investments in small businesses. Pension assets represent the largest sum of money available for investment. We need to develop ways to put that money to work in recapitalizing American businesses, without unduly increasing risks to beneficiaries.

To promote technology transfer, we first must enforce international recognition of the intellectual property rights of U.S. businesses and individuals. Next, we must implement the incentives established in the 1980 Stevenson-Wydler Act, (as amended in 1986)--to commercialize technologies developed in federal labs by giving inventors and lab managers a share in revenues from technology sales. Furthermore, directors of federal labs need to be evaluated on the success of their labs in transferring technology. This will provide them with the incentives necessary to establish the professional marketing function in their organizations, which currently are lacking.

Finally, the Chamber supports the orderly expansion of the Small Business Innovation Research (SBIR) program, assuming that the government's phase two research and development investments produce satisfactory work and SBIR awardees attract adequate investment after the government funding ends. To date, the SBIR program has been an excellent example of the government's levering funds and coordinating efforts to increase desired behavior--in this case, increased private-sector research and development in areas of national scientific interest.

The federal government also performs this levering and coordinating function well in such offices as the Small Business Administration's (SBA) Advocacy Office, the Commerce Department's Office of Productivity, Technology, and Innovation, and the Department of Agriculture's Research Service and Experiment Stations. These are low-budget but "high-intelligence" offices in which the government has developed knowledge to be applied in partnership with other government offices, often at the state and local level, and through the private sector. Programs such as these are important in identifying competitive problems and coordinating efforts to solve them. They could serve as models for other government programs to follow in levering and coordinating private and state and local government resources in addressing important national problems.

III. DEVELOP AND SUPPORT POLICIES AND PROGRAMS TO INCREASE EXPORTS

With all of the macroeconomic and microeconomic problems that small businesses face in becoming exporters, there are those who conclude that increasing exports is an impossible task. However, we have accomplished so-called impossible tasks in the U.S. in the past. Following are the Chamber's recommendations for government and, particularly, for businesses themselves to increase exports.

Recommendation 5 from the WHCSB calls for national policymakers to give higher priority to international trade issues, to reorganize trade functions into a Department of International Trade, to coordinate better export services, represent small businesses more aggressively in international discussions and negotiations, and extend the General Agreement on Tariffs and Trade to include intellectual property rights, services, and agriculture.

Recommendation 35 calls for increasing small business exports by creating an annual, competitive small business export incentive program similar to the highly successful SBIR program (referred to above), to be funded within existing federal international trade programs. This is a creative idea with much promise, which will be studied in the near future in a project commissioned by the SBA Office of Advocacy. We understand Representative Sisisky (D-VA) plans to introduce legislation authorizing such a program.

The Chamber supports this initiative as a cost effective, direct incentive to get small businesses motivated to increase their exports. Recommendation 35 also calls for Small Business Foreign Sales Corporation tax incentives to be improved and for small business export trade programs to be marketed more aggressively through reliance on the private sector.

There is a clear message from the international trade deliberations of the WHCSB, the National Commission on Jobs and Small Business, and the recommendations from the Chamber's Council of Small Business.

First, federal, state, and local export assistance agencies and private organizations dedicated to export development must "coordinate their activities" to be helpful to small businesses. When they are coordinated, these different organizations become more effective in assisting small businesses to cope with the problems involved in building their international markets.

Second, small firms must be encouraged to view international market development as a long-term, non-stop commitment. Today, with the dollar weakening against some currencies, those firms already active in foreign markets are benefiting from doing their preparatory work ahead of time. It takes time to build a name and a distribution system in foreign markets. This "patience factor" must be one of the lessons taught to small firms interested in exporting. If a small business in international competition is not willing to make the commitment to be aggressive, it is giving away a foreign market to a competitor, who will take the foreign market and then invade the domestic market as well.

Third, small businesses must be realistic. Most do not have the product, talent, or financing to become successful exporters. However, those that think they might should seek foreign inquiries and orders, both privately and through the excellent export development programs of the U.S. Department of Commerce and other agencies. When orders begin to come in, then the "part-time" exporter really has to work to understand the foreign market. This means establishing good two-way communications between the company and foreign agents and customers. Phone calls are not enough. Good global marketing depends on frequent person-to-person contact, both overseas and here in the U.S. In addition to communications, servicing the sale is critical. It is essential that the small exporter perform effective after-sale training, customer satisfaction inquiries and, for manufacturers, service and parts support.

Finally, it is most important to have a full-time senior executive in charge of international marketing. This shows an organizational commitment to exporting and creates the incentives and capacity to take advantage of all of the "helping hands" that exist but are sometimes hard to find.

U.S. DEPARTMENT OF COMMERCE

I want to recognize Under Secretary Bruce Smart's leadership at the International Trade Administration (ITA). Smart has continued the sensitive and strong leadership exhibited by Lionel Olmer in having ITA respond to small business's needs.

Despite significant budget cuts in the last two years, ITA has continued to improve its export development, export administration and control, and import administration services.

In export administration and control, the U.S. Department of Commerce has been streamlining the export licensing and administration process for small businesses as required by Congress in the Export Administration Act of 1985. Also, it appears that the Department of Commerce is beginning to win some of the battles within the Administration on export controls. The Chamber considers the relaxation of export controls and streamlining of the process to be extremely important to increase competitiveness. These restraints during the past six years have impeded some of our most technologically advanced companies and have allowed foreign competitors to capture a significant market share in defense technology industries.

In export promotion, because of budget cuts, it appears that ITA is having difficulty providing the level of individual counseling that it has in the past. Through targeted research and computerized information management efforts, ITA is continuing to provide the information on export leads and foreign markets that small businesses so desperately need. The Department of

Commerce can continue to provide export counselling and to promote export awareness by relying more on the private sector. The Department of Commerce has been very effective in levering and coordinating the resources of trade multipliers, such as export management companies, export trading companies, trade clubs and chambers of commerce, and big businesses. Just as the SBA has been increasing reliance on the private sector in its business development programs, so the Department of Commerce can reemphasize these sources of export assistance. The Department of Commerce's planned export promotion campaign involving the "Ad Council" is a perfect example of an innovative effort in this area.

We strongly encourage the Department of Commerce to do more to encourage federal-state-private initiatives to improve the coordination of export development services. The Chamber would be pleased to take the lead in inviting private sector representatives to participate in such discussions. The Chamber strongly supported a pilot program within the U.S. & Foreign Commercial Service (U.S. & F.C.S.) called the State Agenda for Exports program, begun in 1983 and ended in 1986. This program led to a major export finance and promotion initiative in the State of Illinois and to increased export development initiatives in more than 20 other states. It is important that the Department of Commerce concentrate some of its resources on developing state export programs for small business.

EXPORT-IMPORT BANK

The Chamber has supported the small business set aside and the small business marketing initiatives at the Export-Import Bank (ExIm Bank) begun in 1983. These initiatives are producing results in increased direct loans and guaranteed loans by commercial lenders in the ExIm Bank's export finance network. I want to commend ExIm Bank Chairman John Bohn's leadership on small business issues as described in his statement to this Committee last week. It is clear that the Ex-Im bank is getting results from its direct loan, guaranteed loan and insurance programs for small business.

However, the ExIm Bank is not constituted to meet all or even most of the export financing needs of U.S. small businesses. It does not have the resources or the distribution system to educate commercial banks all across the U.S. on the intricacies of export financing, nor, with its limited staff, could it process or underwrite a large volume of guaranteed and direct loan applications on a scale approaching the size of the SBA loan program, for example.

The challenge of generating more export and working capital financing by regional and local banks can be accomplished best through the private sector, motivated and subsidized at the state level, if necessary. The Illinois Export Council, chaired by Lieutenant Governor George Ryan, and the Illinois Export Development Agency are excellent examples of such a public-private partnership.

SBA INTERNATIONAL TRADE PROGRAMS

The Chamber supports the Administration's and this Committee's reassessment of the SBA's International Trade Office. Because the SBA has such a small international trade budget--less than $900,000--it should concentrate on information dissemination and education support to identify potential small business exporters and to link them with needed information and assistance. There are many creative ideas and initiatives emerging from business, export trading companies, trade clubs, port agencies, state and local governments, and federal agencies, including "Export SBIR."

The International Trade Office could play an important role in disseminating these small business ideas and programs and in coordinating activities and ideas among private and public export development organizations. We recommend that the SBA convene a national conference on "Coordinating Small Business Export Assistance" in the near future. The Chamber would be pleased to assist in sponsoring such a conference.

We commend the Deputy Administrator's initiative to have the SBA's National Advisory Council's International Trade Committee meet with the SBA's international trade staff and business development experts to develop improvements in service. This meeting is taking place today, March 24, 1987. The Chamber and the U.S. and F.C.S. have engaged in a similar exercise, in which a business task force of Chamber members reviewed the U.S. & F.C.S.'s programs and suggested improvements. The Chamber would be pleased to offer assistance to the SBA as well.

DEPARTMENT OF INTERNATIONAL TRADE

There is a multiplicity of trade program and policy offices in the federal government, including the Department of Agriculture, The U.S. Trade Representative, and the Department of State, in addition to the programs discussed above. Accordingly, the Chamber supports, in principle, the consolidation of many federal trade functions into a Department of International Trade, and we are studying how this could be implemented best. Despite improvements in the different agencies' small business programs, future improvements have to be made more rapidly, and limited resources have to be coordinated better. It seems that a Department of International Trade is the best institutional mechanism to make this happen.

IV. PRESS FOR THE ELIMINATION OF FOREIGN TARIFFS AND NON-TARRIFF BARRIERS TO U.S. TRADE AND INVESTMENT

Problems with trade, like our other major national problems, cannot be solved by passing a law or by the federal government's acting alone. On the other hand, American business alone cannot reverse our current position in world trade. SBA Chief Counsel for Advocacy Frank S. Swain's testimony last week summarized very well the attitudes U.S. small businesses have regarding international trade. They thrive on competition and are overwhelmingly in favor of free, but fair, international competition and are opposed to protectionist legislation. To accomplish this, the U.S. government must demand a level international "playing field." The Chamber continues to urge tougher enforcement of trade laws and identification and removal of market access barriers. The Chamber is monitoring the Administration's use of Section 301 of the Trade Act of 1974 to end such barriers, and we support mandatory Presidential retaliation when trade agreements are violated.

I would like to congratulate the Chairman and the members of the Committee for their initiative in adding a small business title to H.R. 3. We understand that this Committee's contributions to the bill will be limited to programs under the Committee's jurisdiction. However, through these hearings you are providing an excellent service to the Congress and the small business community by eliciting small business's views on the major policy issues of the day. The Chamber looks forward to continuing to assist you in any way possible in this area.

We view H.R. 3 as a starting point towards achieving the four competitiveness objectives outlined earlier.

Mr. Chairman, the enactment of constructive trade legislation this year can contribute significantly to correcting some of our trade related problems. But we must be realistic as to what it can and cannot do. There are major macroeconomic issues, such as the budget deficit, third world debt, and growth rate differentials and exchange rate instability among the industrialized nations, that present serious problems that are not amenable to solution through trade legislation.

H.R. 3 does include a number of positive provisions that are consistent with our objectives, including:

A. Strengthened telecommunications market access provisions;
B. New trade agreement negotiating authority;
C. Clarification of the Foreign Corrupt Practices Act;
D. Improved procedures for the Export-Import Bank;
E. Strengthened intellectual property rights protection;
F. Mandatory retaliation against foreign unfair trade practices.

However, the bill also includes a number of objectionable provisions that would undermine our position in the world trading system.

Two of those provisions would include:

- The so-called "Gephardt amendment," which would mandate U.S. retaliation on the basis of a unilateral determination that other countries' trade surpluses are "excessive and unwarranted." This amendment would likely violate U.S. GATT obligations, provoke swift retaliation, probably raise prices, and could create shortages in affected sectors and ultimately reduce trade opportunities for U.S. companies.
- Inclusion of "internationally recognized workers' rights" (such as rights to association, organization, collective bargaining, prohibition on forced or compulsory labor, minimum employment age, and "acceptable conditions" with respect to minimum wages, work hours, and occupational safety and health) as a condition to be considered by the Administration in taking retaliatory action; such a condition is highly arbitrary and would be unworkable.

For a detailed discussion of the major provisions of H.R. 3, I would call the Committee's attention to the February 18, 1987 statement by William T. Archey, the Chamber's Vice President for International Policy, before the Subcommittee on Trade of the House Committee on Ways and Means. Mr. Chairman, with your permission, I would like to submit that statement for the hearings record.

V. IMPROVE THE ABILITY OF U.S. FIRMS TO COMPETE DOMESTICALLY BY PROVIDING EFFECTIVE DOMESTIC RECOURSE TO FOREIGN UNFAIR TRADE PRACTICES AND INJURIOUS IMPORTS

The U.S., which has been a major factor in building the current international trading system, has talked about enforcing fair trade in international negotiations but has not done nearly enough to enforce the legal rights of American small businesses suffering from unfair and illegal imports.

In his testimony last week, Mr. Smart described the Department of Commerce's Office of Investigations, which has taken 16 small businesses through the trade relief process so far in 1987. Unfortunately, most small businesses do not even know that they may be entitled to import relief. Even when they know that they may have a case, they are often intimidated from proceeding by the expense, effort, and uncertainty of the outcome. We understand that Representative Ridge (R - PA.) has introduced a bill, H.R. 1737, to address this issue, and will be testifying before this Committee next week.

Currently, the Chamber is studying ways to alleviate this situation, based on recommendations advanced by its Council of Small Business. They include barring repeat offenders of import laws from importing goods and services; requiring that the Customs Service notify the ITA and attorneys for petitioners who successfully have brought anti-dumping cases when it initiates an investigation relating to items subject to anti-dumping or countervailing duties; and compensating petitioners who have brought successful anti-dumping cases for their reasonable expenses, to be paid from funds resulting from the imposition of the new duties. This would be similar to the compensation that small businesses may receive when they successfully challenge unfair actions by the government under the Equal Access to Justice Act.

As I mentioned earlier, the Chamber supports mandatory retaliation against nations when trade agreements are violated, and the Chamber supports expedited action by the Department of Commerce, Customs Service and International Trade Commission on behalf of individual small businesses when they are affected by unfair imports.

VI. CONCLUSION: THE PRESIDENT'S COMPETITIVENESS INITIATIVE

The Chamber believes that the President's Competitiveness Initiative is a comprehensive and reasonable approach to assure American competitive preeminence into the 21st century. In its six major parts, including education and training, science and technology, intellectual property protection, legal and regulatory reform, international market development, and federal spending control initiatives, the bill addresses the special needs of small business, as well as the more general concerns of U.S. exporters.

Without going into detail on the specific proposals, the Chamber believes that they, by and large, address the four objectives that the Chamber considers critical to international competitiveness: domestic policies for growth; export development policies and programs; market access initiatives to reduce foreign tariffs and non-tariff barriers; and more effective domestic recourse to unfair trade practices and injurious imports.

Attached as (Exhibit 1) is the Chamber's summary of the Competitiveness Initiative with the Chamber's positions on the specific recommendations, except for the international market development recommendations. The Chamber supports most of the recommendations, opposes none, and is studying the new recommendations. Based on our understanding of the trade recommendations, particularly from Mr. Smart's testimony last week, I believe that they deserve strong support and are consistent with Chamber policy.

That concludes my statement. I would be pleased to respond to your questions.

EXHIBIT 1

U.S. Chamber of Commerce

Washington, D.C. 20062

The President's Competitiveness Initiative

The President's Competitiveness Initiative is the Administration's proposal for assuring American competitive preeminence into the next century. It calls for actions by business, workers, government and families and individuals. The initiative mixes rhetoric and a limited number of new programs to create momentum for the Administration's dealings with Congress on issues such as protectionism and deficit reduction.

The Competitiveness Initiative consists of six major parts dealing with items ranging from school programs to eliminating the federal deficit. The President has called it his "quest for excellence plan" and it involves 43 specific action points under the six major program divisions. This paper outlines the five areas other than trade which make up the Initiative.

THE PRESIDENT'S COMPETITIVENESS INITIATIVE SUMMARY

PART I. INCREASING INVESTMENT IN HUMAN AND INTELLECTUAL CAPITAL

This section deals with education and training issues and includes proposals to:

1. Improve Basic Skills: The Department of Education will distribute case studies on effective programs. (Chamber supports.)

2. Raising Standards: The Administration is proposing a minimum high school program that includes four years of English, three years of math, science and social studies, and a demonstrated proficiency in the use of computers. (Chamber supports the concept with reservations over imposing federal standards on state and local school boards.)

3. Helping Needy Schools and Youth: The Administration will recommend the reauthorization of Chapters 1 and 2 of the Education Consolidation and Improvement Act to target resources to disadvantaged schools and youngsters and foster innovation and reward success. (Chamber supports.)

4. Promoting Literacy: The President proposes establishing the year 2000 as the target date for dramatic reductions in illiteracy. The Administration will also propose reforms in bilingual education. (Chamber supports.)

5. Instilling Productive Habits and Values: This concept includes working for drug free schools, studying the basic documents of our national heritage and fostering "moral literacy." (Chamber supports drug education programs and has no position on other topics.)

6. Assisting Dislocated Workers: The President will propose a $1 billion worker adjustment program to: (a) help 700,000 additional dislocated workers, (b) offer counseling, job search assistance, basic education and job skill training, and (c) provide early training and adjustment opportunities for workers. (Chamber supports.)

7. Creating Opportunities for Needy Youth: The President will propose an $800 million youth employment program. (Chamber supports.)

8. Providing Greater Opportunities Through Work (GROW): The President will propose a new program to encourage employment and training proposals for welfare (AFDC) recipients. (Chamber supports.)

9. Improving Labor Mobility: The Secretary of Labor will study private pension reforms to reduce barriers to labor mobility. (Chamber has no position.)

10. Seeking Unemployment Insurance and Employment Service Reforms: The President will propose reform in these two areas to give the state greater flexibility. (Chamber currently has no position, but the U.C. Council is reviewing this topic.)

PART II. PROMOTING THE DEVELOPMENT OF SCIENCE AND TECHNOLOGY

The purpose of these proposals is to generate new knowledge in advanced technologies, swiftly transfer new technologies to the marketplace and expand the Nation's talent base in science and technology. (Chamber supports.)

11. Establishing Science and Technology Centers: The President will propose establishing a limited number of interdisciplinary "Science and Technology Centers" at different universities. (Chamber supports.)

12. Funding the National Science oundation: The President will propose doubling the National Science Foundation over the next five years. (Chamber supports.)

13. Creating a Technology Share Program: The President will direct the Departments of Agriculture, Commerce, Energy, Health and Human Services, and the National Aeronautics and Space Administration to join with universities and private firms in joint basic and applied research projects. (Chamber supports.)

14. Initiating People-to-People Program: The President proposes an interchange of government and private scientists and engineers. (Chamber supports.)

15. Increasing Federal Technology Transfers: The President will issue an Executive Order to improve industry access to federal science and technology enterprises. (Chamber supports.)

16. Ensuring Incentives for Private R&D: The President will seek legal and regulatory stability for R&D tax credits. (Chamber supports.)

17. Increasing Scientific Literacy: The President is directing the National Science Foundation and other federal agencies to work with educators to improve scientific literacy and increase interests in careers in science and engineering. (Chamber supports.)

18. Pursuing Key 1988 R&D Initiatives: The President proposes a 12 percent increase in federal R&D spending with a focus on the following projects - a space station, a hypersonic aircraft, civil space technology, geosciences, plant sciences program, manufacturing technology, synchrotron light source facilities, hyper speed integrated circuits, and mapping human DNA. (Chamber supports.)

19. Accelerating Defense Spin-Offs: The President is directing the Department of Defense to accelerate the effort to "spin-off" technologies from their research programs to the private. (Chamber supports.)

20. Promoting a Private Sector Space Industry: (Chamber supports.)

21. Commercializing Federal Technical Information: The Administration will establish a new policy to encourage the commercialization on non-potentable federal research in areas such as software and engineering drawings. (Chamber supports.)

PART III. BETTER PROTECTION OF INTELLECTUAL PROPERTY

The purpose of this section is to provide a framework to protect those who develop new ideas, products and services.

22. Enact Omnibus Intellectual Property Reform: This will include encouraging the licensing of patented technology, raising protections for products resulting from a patented process and restoring the term of patents covering agricultural chemical products and animal drugs to five years. (Chamber has no position.)

23. Protecting Copyrights: The Administration seeks a solution to unauthorized copying of copyright material on digital audio tape recorders. (Chamber has no position.)

24. Protecting Business Confidentiality: The President will issue an Executive Order to protect business confidentiality under the Freedom of Information Act (FOIA). (Chamber supports.)

25. Reforming FOIA: The President will propose statutory reform of the definition of trade secrets and confidential commercial information under FOIA. (Chamber supports.)

26. Sharing Patent Files: The President is directing the Patent and Trademark Office to share its English language abstracts of Japanese and European patents with the private sector. (Chamber supports.)

27. Joining the Berne Convention: The Administration will propose joining the Berne Convention for the Protection of Literacy and Artistic Works.

28. Protecting U.S. Intellectual Property Abroad: The President is directing U.S. negotiators to consider protection of U.S. intellectual property rights in their activities.

PART IV. ENACTING ESSENTIAL LEGAL AND REGULATORY REFORMS

Outmoded rules and regulations self-imposed disincentives place the U.S. at a competitive disadvantage in a global marketplace. The Administration is proposing the following reforms:

29. Enacting Product Liability Reform: The Administration's legislative proposal includes - Retaining a fault - based standard, reforming joint and several liability, limiting noneconomic damages, allowing use of periodic payments of damages, reform of collateral source rule, impose sliding scale for attorney's fees and encourage the use of alternative dispute resolution mechanism. (Chamber supports.)

30. Enacting Antitrust Refinements: The Administration proposes statutory reform in the antitrust area for the following areas - pro-competitive mergers, limiting damages to actual amounts rather than treble damages, removing unwarranted restrictions on interlocking directories, clarifying the application of antitrust law in international trade cases and reducing claims for damages to reflect partial settlements. (Chamber supports.)

31. Improving Export Controls: The President is directing the Cabinet to undertake a review of the export controls program and report to him in March.

32. Pursuing Regulatory Relief: The President has requested Vice President Bush to direct the Task Force on Regulatory Relief to review the federal regulatory structure from the viewpoint of its impact on competitiveness. (Chamber supports.)

33. Providing Competitive Financial Services: The Administration is proposing the following steps to modernize our financial institutions laws - implement the recommendations of the Vice President's Task Force on the Regulation of Financial Services; recapitalize to the FSLIC (the Federal Savings and Loan Insurance Corporation); and conduct a comprehensive reform of our 50 year old regulatory system for financial institutions. (Chamber supports in concept.)

34. Deregulating Transportation and Natural Gas: The Administration is proposing complete deregulation if surface transportation other than railroads and will oppose efforts to re-regulate air and rail transportation. (Chamber supports current deregulatory status in transportation.) Further, the President will propose full deregulation of pricing and transportation of natural gas (Chamber supports), and in addition, he will recommend oil pipeline deregulation. (Chamber has no position.)

35. Strengthening the Private Pension System: The Administration will propose ERISA (Employee Retirement Income Security Act of 1974) reforms to - reduce overfunding (Chamber supports), permit employers to use excess assets for health benefits for current retirees (Chamber supports), and make ERISA less lenient with underfunded systems. (Chamber has no position. This is a major concern for GM because its pension is underfunded.)

PART V. SHAPING THE INTERNATIONAL ECONOMIC ENVIRONMENT

The President has prepared a comprehensive program in this area that is currently under review by the Chamber.

PART VI. CONTROLLING FEDERAL SPENDING

The President remains committed to the Gramm-Rudman-Hollings deficit target and urges the Congress to pass his budget. (Chamber supports Gramm-Rudman-Hollings.) The Initiative does not provide detailed spending recommendations.

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NEWS

FOR IMMEDIATE RELEASE

Contact: Frank Benson

FOUR BASIC NEEDS FOR BOOSTING SMALL FIRMS' COMPETITIVENESS NAMED BY U.S. CHAMBER CHAIRMAN IN STATEMENT TO HOUSE GROUP

WASHINGTON, March 24 -- U.S. Chamber of Commerce Chairman Edward Donley today described a four-point program to strengthen the nation's small business firms both domestically and in world markets, at a Congressional hearing.

In testimony before the House Small Business Committee, Donley, the Chamber's top elective official, presented the business federation's recommendations on the federal government's role in developing an internationally competitive climate for small entrepreneurs. Donley, chairman of the executive committee of Air Products and Chemicals, Inc., Allentown, Pa., noted that his own firm began as a small operation and today, in large part due to its exports, is one of the nation's 250 largest industrial firms.

The Chamber continues to advocate tough actions by the government in order to get a level "playing field" in international trade, he stated. "But, an even higher national priority is to improve programs that will foster increased exports," the Chamber official declared.

Specifically, Donley singled out four broad basic objectives the Chamber feels are needed in developing domestic and international trade policies that would make the country's businesses more competitive. These are:

1. Remove domestic disincentives to business performance;
2. Develop and support policies and programs to increase exports;
3. Eliminate foreign tariff and non-tariff barriers to U.S. trade and investment; and
4. Provide effective domestic recourse to foreign unfair trade practices and injurious imports while ensuring U.S. consumers access to fairly-traded goods and services.

Donley commended the committee members for including a small business title, H.R. 3, in trade legislation before the Congress, but cautioned that the trade bill cannot solve U.S. competitiveness problems until major macroeconomic issues, in particular the federal budget deficit, are brought under control.

Donley reviewed the increasing number of anti-small business initiatives in the 100th Congress, including mandated benefits, increases in the minimum wage and a lack of progress on national product liability standards, and also shared with the committee the Chamber's view on capital formation and technology transfer policies important to small businesses.

Additionally, Donley described the Chamber's views on export promotion policies and reviewed small business programs in the Department of Commerce, Export Import Bank and Small Business Administration, concluding that better coordination and levering of public and private resources is needed. Donley also stated that the SBA should convene a national conference, with U.S. Chamber assistance, on "Coordinating Small Business Export Assistance." Finally, the U.S. Chamber's chairman presented the business federation's views on the trade bill, H.R. 3, and on additional market access and import relief recommendations advocated by the Chamber. Donley stated the Chamber's support for President Reagan's Competitiveness Inititative and urged the Small Business Committee to work to enact its basic principles.

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NOTE TO CORRESPONDENTS: For a complete copy of the Donley statement, contact the Chamber News Department, 463-5682.

Prepared Statement of Virginia Littlejohn, Chairman of the Committee on Economic & Regulatory Issues, Small Business Legislative Council

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Jewelers of America
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Mechanical Contractors Association of America, Inc.
Menswear Retailers of America
National Association for the Self-Employed
National Association of Aircraft and Communication Suppliers
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National Association of Catalog Showroom Merchandisers
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National Association of Investment Companies
National Association of Manufacturing Opticians
National Association of Minority Contractors
National Association of Personnel Consultants
National Association of Plumbing-Heating-Cooling Contractors
National Association of Realtors
National Association of Retail Druggists
National Association of Small Business Investment Companies
National Association of the Remodeling Industry
National Association of Truck Stop Operators
National Association of Women Business Owners
National Candy Wholesalers Association
National Chimney Sweep Guild
National Coffee Service Association
National Council for Industrial Innovation
National Electrical Contractors Association
National Fastener Distributors Association
National Grocers Association
National Independent Dairy-Foods Association
National Moving and Storage Association
National Office Products Association
National Parking Association
National Precast Concrete Association
National Shoe Retailers Association
National Society of Public Accountants
National Tire Dealers & Retreaders Association
National Tooling and Machining Association
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National Venture Capital Association
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Retail Floorcovering Institute
Small Business Council of America, Inc.
Smaller Manufacturers Council
Society of American Florists
Specialty Advertising Association International
United Bus Owners of America
Web Sling Association

My name is Virginia Littlejohn and I am the Chairman of the Small Business Legislative Council (SBLC) Committee on Economic & Regulatory Issues, Vice President for Appointments of the National Association of Women Business Owners, an SBLC member, and Executive Director of the Professional Services Council, representing the professional and technical services industry. SBLC is an independent, permanent coalition of ninety trade and professional associations who share a common concern for the future of small business. Together, our member associations represent the interests of over four million small businesses. The unique characteristic of the SBLC is that we represent nearly every segment of the economy and we do so through the associations. As a result, we quickly focus on how a public policy will effect different segments of the economy. However, we have never lacked issues upon which we all agree. The common denominator of small business and entrepreneurship is a strong bond. Our diversity, combined with our common commitment, permits us to offer a unique perspective on the concerns of the small business community.

Competitiveness has become the major buzzword in Washington since late 1986. As the debate on international competitiveness has accelerated, users of the term ascribe to it multiple definitions, running the gamut from free trade to protectionism. Despite the conflicting definitions, the issue of what public and private policies can best enhance the competitive prospects of U.S. business is absolutely fundamental to America's future.

International competitiveness should provide a clarion call to new purpose and resolve, a new challenge for us to rise to, just as America rose to the Sputnik challenge in 1957. The Soviets' great triumph in space became a test of America's ability to educate and train its people, and to adapt new technologies, successfully culminating with our putting a man on the moon in 1969.

The current challenge is even greater, because what we face now has far more sweeping impact on our lives than the national humiliation of Sputnik. Foreign competitiveness gnaws at the very fabric of American life -- taking away jobs and reducing income; hurting families and increasing alcoholism, child and spouse abuse; depressing villages, cities, state and regional economies; and devastating whole economic sectors.

In addition to the specific issues raised by Chairman LaFalce in his letter requesting testimony today, which I have addressed in my written remarks, there are several additional issues of overwhelming importance to international competitiveness which I will address verbally, because I believe they provide a context for the rest of the debate to be meaningful.

Inadequate Data and Statistics

First and absolutely fundamental, is the inadequacy of America's economic data and statistics. Since the end of the Second World War, our economy has undergone major transformations, from being primarily a manufacturing economy to a services and information economy. These rapid changes require effective management, but it is impossible to manage anything effectively if we do not understand its dimensions.

While the federal government produces bales of statistics, comparatively little useful information is available on economic growth, innovation, trade and productivity in emerging sectors of the economy. Lack of sound data is a practical barrier to understanding the nature, dimensions and character of the new American economy and its dynamic entrepreneurial sector.

Management expert Peter Drucker has stated, "The aggregates on which all statistics are built are now 50 years old. And so the great national economic aggregates have been reliable plus or minus 40 percent...If you get that much slippage and still base policy on it, your chances of doing the wrong things are simply too great."

Policymakers trying to formulate appropriate trade, tax, procurement and other policies are not the only ones who need realistic information to do their jobs effectively. In addition, America's private sector, struggling to meet the challenges of a new global economy, clearly needs realtime information to better understand the changing marketplace, to identify emerging market niches, and to prepare realistic business forecasts and projections which will enable them to compete.

A prime example of inadequate data is the professional and technical services industry. Until January 1987, the Standard Industrial Classification (SIC) code did not contain a rational classification system for professional services firms; in fact, a majority of the industry was listed as "Services Not Elsewhere Classified." With the 1987 SIC code revision and new numbers assigned to this industry, preliminary research indicates that instead of the $35 to $70 billion industry that industry experts had thought, the sector instead is at least a $165 billion a year industry. Rather a considerable difference! To marginally revise our Standard Industrial Classifications at 15 year intervals is a national disgrace, in an era when whole industries are born and die over the span of a decade!

The impact of inadequate data and statistics can be quite profound when applied to such important public policy issues as the U.S. trade deficit. Preliminary data for 1986 show last year's trade surplus in services averaging about $44 billion, helping to offset the deficit in goods trade of almost $150 billion. The government of Canada recently reported that America's surplus trade in selected services with Canada was many billions of dollars higher than the United States had reported--essentially double what we had believed because of our wretched statistics.

Congress' Office of Technology Assessment, in a report published last year called Trade in Services: Exports and Foreign Revenues, estimated that "as much as half of the Nation's exports of services may escape the official statistics" -- for example, "computer software, one of the most critical service-related products in a high-technology economy."

Citing the difficulty of trying to come up with real numbers, statistical expert David Birch of MIT commented ironically several weeks ago that perhaps our international trade in services data are so understated that we don't even have a trade deficit! It is chilling to even contemplate that our raging trade skirmishes and great national trade debate might be based on flawed conclusions derived from deeply flawed data.

Until America gets serious about updating its statistical aggregates, which reflect a 1930s' world view, we will never be able to realistically measure where we've been, or where we're going, or know when we've gotten there. As baseball legend Casey Stengal said, admittedly in a slightly different context, "If you don't know where you're going, you might end up someplace else."

Export Enhancement through Education

A second central issue concerns export enhancement, but in a broader context, perhaps, than the Committee had intended for us to focus on today. A cornerstone of enhancing America's ability to compete in the global marketplace is making a substantive investment in our human capital through education, training and retraining, via pre-school, grade school, high school and college, and continuing education. Constantly improving the quality of our workforce by arming our people with the necessary knowledge is essential to making America competitive.

D. Bruce Merrifield, Assistant Secretary for Productivity, Technology and Innovation at the Department of Commerce, states the problem bluntly: "Lifelong reskilling of the workforce will now become a critical problem because any set of skills may be obsolete in 5 to 10 years. The great frontier of American education is now going to start at 22, after we get out of school, and continue all our lives."

There are many glaring deficiencies in the area of training. Some have been expertly explained in the report, A Nation at Risk, and in the recommendations of the Carnegie Forum on Education and the Economy. While preliminary steps have been taken to address some of these problems, glaring deficiencies remain. There has been no **sustained** public policy toward training to support vocational schools, community colleges and public service employment. The federal government has adopted and abandoned an astonishing14 different training programs since1962. And our supply of engineers and technical specialists is shrinking rapidly. The National Commission on Small Business and Jobs estimates that by the year 2000 we may have a shortage of 15 million scientists, engineers, skilled mechanics and semi-skilled workers.

To redress this crisis-in-the-making, America must make a renewed commitment to educational standards of excellence which emphasize educating American students on economic forces, entrepreneurship, international issues, foreign languages, mathematics, science, and training them to manage and "mentally retool" in periods of massive change and technological innovation. This can be accomplished through a variety of mechanisms including,

- business-education partnerships with business leaders supporting local schools and colleges with their time, knowledge, and real-world career guidance that will teach them about flexibility and coping with change,
- magnet schools for students gifted in math and science, and
- grants to stimulate students to enter careers in engineering, sciences, mathematics and teaching of these subjects.

Another key education issue is our inability to understand the language or culture of countries we are trying to compete with. This is compounded by the paucity of managers trained in global trading issues. A survey by Egon Zehnder, a large worldwide management recruiting firm, of 100 top managers of major companies found that 66 percent of those surveyed agreed that American managers were "woefully ignorant about foreign markets." Unfortunately, this percentage would be far higher if executives of small and mid-sized businesses were surveyed.

Effectively educating managers on foreign markets, language and culture is essential to export enhancement. Establishing corporate training programs to address this deficiency is vital to our long-term success in competing with foreign firms. This is a challenge for small and mid-sized firms, as well as larger firms. CEOs of firms of every size must be aware of potential recruiting problems with finding skilled foreign managers, and start now to redress this gap.

One superior mechanism already exists, which if expanded, could greatly enhance the ability of American business to understand foreign business practices.

Expand Fulbright Program to Business and Industry

For forty years the Fulbright Program has supported an exchange of American students and academic scholars with students and scholars from other nations. The benefits in international understanding from that program have been incalculable. The time has come to expand the Fulbright exchanges to include individuals in business and industry, to provide an opportunity for Americans in business to learn about other cultures and how we may work more effectively in a global economy.

The Fulbright program could be expanded to include a component for international business exchanges, open to people from firms of all sizes and types, with options that offer:

- Short-term exchanges of three to six months, with an intensive language and cultural training program to precede these exchanges; and
- Full-year exchanges along the line of the traditional Fulbrights, again preceded by an intensive language and cultural training program.

These exchanges should not be limited to the countries of Western Europe but should include Latin America, the Pacific Rim and the Far East, Africa and the Middle East.

Restoring our "Yankee Trader" Tradition

I applaud your leadership and vision, Chairman LaFalce, in calling for the creation of a National Commission on Small Business and Jobs. Countless superior recommendations which we endorse emerged from the Commission report related to regaining our "Yankee Trader" tradition, including the following:

-Expanding the scope of the General Agreement on Tariffs and Trade (GATT) to include services, agriculture and intellectual property rights, as well as greater consideration of small and mid-sized businesses in GATT (regarding intellectual property, SBLC would also urge revision of those laws which protect intellectual property rights to stop the "theft" of American ideas by others in the world market. Much of our technology is frequently the basis upon which our world competitors build their own export base -- at our expense);

- Improve and simplify the Foreign Sales Corporation provisions to make it more useful to smaller firms;

- Require Eximbank to market its existing small business export financing programs more aggressively, and encourage states to do so too;

- Create a Small Business Exporting Incentive program patterned along the lines of the trailblazing Small Business Innovation and Research program;

- Seek methods under GATT to allow U.S. exporting companies cost reductions through tax incentives to match the tax incentives available to foreign businesses;

- More aggressively disseminate information concerning programs of the International Trade Administration (ITA) already available to smaller firms, working through existing business groups (parenthetically, I have worked closely with federal agencies on two services trade missions led by the National Association of Women Business Owners, one to Europe, one to Japan, and the quality and amount of assistance provided by both Commerce and SBA's Office of International Trade have been truly superior. I only wish that more small and mid-sized business people knew about them);

- Reorient ITA export promotion programs to focus specifically on small and mid-sized business participation;

-Actively assist the formation of Export Trading Companies;

-Create incentives for multinational corporations to use U.S. small and mid-sized businesses as subcontractors in overseas projects;

-Provide incentives for large companies to assist small and mid-sized U.S. companies abroad by use of facilities and market leads;

- Develop an International Commerce Business Daily to provide marketing leads to small and mid-sized firms nationwide, and

- Establish a public-private partnership to provide market information and analysis to the business community, similar to that provided by the Japanese External Trade Organization (JETRO).

We believe there are many resources already on hand to enhance the small and mid-sized business owner's ability to compete in the export market. We need to publicize these resources, focus their energies and turn them loose. As an example, in addition to the trade-oriented offices at Commerce and SBA, the Small Business Development Center (SBDC) program should be upgraded to include more activity in preparing small and mid-sized businesses for the export program. In recent years, the SBDCs have developed into effective "maximizers" of public/private resources, and SBLC would support enhancement of their role in the export assistance arena.

At the federal level, creation of a cabinet agency on international trade would eliminate the current confusions and overlap in federal agencies on trade issues, and help unify our trade policy and activity. If this ultimately proves infeasible, the President should take steps to make the system less labyrinthine by eliminating bureaucratic overlap and correcting indecisiveness in our trade policy so that companies of all size can better access the system.

The federal government, however, is only one player among many. State and local leadership is also vital to encouraging exports and increasing competitiveness.

The Continuum Between Domestic and International Markets, and Domestic Barriers that Undercut International Competitiveness

Those of us in the private sector familiar with the federal procurement process consider it seriously flawed, and an example of federal regulation at its worst. The procurement laws, rules and policies, as presently framed and implemented, produce major inefficiencies and dislocations. This is particularly unfortunate because effective utilization of federal procurement -- a $200 billion annual market for goods and services -- is one of the most direct ways in which government can stimulate innovation, productivity and competitiveness in the American economy.

To do so, steps must be taken to streamline and simplify procurement, while at the same time opening up access to smaller firms, and providing incentives for those firms to grow and to move into international markets.

Unfortunately, it appears at times that many policymakers do not comprehend the relationship between domestic policies and international competitiveness. While in one breath they state their ardent support for expansion of international trade in services, in the next breath they cripple that very sector through flawed procurement policies.

Recently, for example, the federal government disallowed the expenses for professional and technical services firms travelling to France for the Paris Air Show, the most sophisticated in the world, and a critically important marketing forum for smaller American companies trying to break into international trade in aerospace and related sectors.

Similarly, the professional and technical services industry is currently taking body blows as the result of an interim rule on profit policy recently issued by the Department of Defense, which was designed to reduce defense contractor profits by one profit point, as well as to encourage investment in capital equipment so as to increase productivity. Because the professional and technical services industry's investment is in human and intellectual capital rather than in capital equipment, these companies face profit reductions of 20 to 50 percent if the profit rule is not changed, according to a recent study of companies in this sector.

Policymaking, via both statute and regulation, that doesn't recognize the continuum between domestic and international markets is shortsighted at best. The $165-billion-a-year U.S. professional and technical services industry is the world's most highly developed -- at the cutting edge in such fields as software development, artificial intelligence, systems design and integration, and test and evaluation -- with probably a 5-10 year competitive lead over Japan and other industrialized countries in a number of sectors. Federal policies should nurture and support this and similar dynamic new industries, not erect obstacles and barriers that undercut them domestically and damage their quest for potential exports.

Privately Funded Commission to Look at the New American Economy

One way to dramatically highlight this issue and related problems is with a congressional call for a commission to be funded by the private sector, as was the National Commission on Small Business and Jobs. Such a commission would review the state of data and public policy with relationship to the new services, information and technology-driven economy, with particular emphasis on technology-based industries and highly skilled sectors that enhance our competitiveness in the world economy.

To continue to dismiss America's "services economy" as one where people take in each other's laundry and serve each other Big Macs demonstrates a profound lack of understanding of the new American economy, and the enormous synergy between services and manufacturing.

Trade as a Top SBLC Priority

As you know, just six weeks ago, SBLC held its annual isssues conference. At that meeting our members reviewed dozens of possible issues of concern to small business. After a day of debate, we voted on our priorities for the 100th Congress. Our sixth priority for 1987 was as follows:

STATEMENT OF INTERNATIONAL TRADE POLICY. The participation of small businesses in the international market represents an important and fundamental criterion for the resurgence of the United States trade position. The following areas must be addressed and policies adopted in order to ensure "fair" trade for U.S. firms in the world market:

a. Financial and management assistance to enable more small businesses to compete in the international market.

b. Removal of barriers to international trade, such as licensing, specification and nationality requirements not otherwise imposed on domestic firms.

c. Measures to encourage small firms to export, such as stronger patent and proprietary data protection as well as programs to assist firms to convert to the metric system.

d. Stricter and more thorough enforcement or improvement of current United States fair trade laws.

e. Adoption of a clear and forceful international trade policy, either through creation of a cabinet level position or enhanced coordination and focus of current policymakers.

f. A right of private action with compensation to the injured party should be created to enable access to remedies by small business. A "short form" expedited, low cost proceedings before the ITC should be established.

g. The Standard Industrial Classification (SIC) code should be massively overhauled so that it will evolve with the continuing diversification and growth of the American economy, and provide timely information to policymakers and business users. In addition, a Commission on Services, Information, and High Technology should be created by Congress to recommend statistical, trade, tax, procurement and other policies which will enhance America's competitiveness, both internationally and domestically.

Conclusion

As noted earlier, Washington's biggest buzzword in years, "competitiveness," means markedly different things to different people. How we ultimately define it will be a test of our vision, our leadership and our national resolve. Because of your leadership, Mr. Chairman, this Committee for the first time provides a unique forum to help define the term, sharpen the debate and force the pace. Go to it with a vengeance, because our economic future depends on it!

Thank you.

Prepared Statement of Hon. Nicholas Mavroules, a Representative in Congress from the State of Massachusetts

THANK YOU MR. CHAIRMAN. I WOULD LIKE TO EXPRESS MY APPRECIATION TO YOU FOR CALLING THESE HEARINGS, AND FOR THE INITIATIVES YOU HAVE TAKEN IN THE AREA OF COMPETITIVENESS. THROUGH YOUR EFFORTS, THE VOICE OF THE SMALL BUSINESS COMMUNITY WILL BE HEARD WHEN THE FULL HOUSE OF REPRESENTATIVES BEGINS CONSIDERATION OF THE TRADE LEGISLATION. MR. CHAIRMAN, I BELIEVE THAT I SPEAK FOR ALL MEMBERS OF THE COMMITTEE WHEN I SAY THAT YOUR EFFORTS IN THIS AREA ARE TO BE COMMENDED.

AS WE LOOK FOR WAYS TO IMPROVE OUR COMPETITIVE EDGE, I THINK THAT WE WOULD BE WELL SERVED BY EXAMINING RECENT SUCCESSES IN MY HOME STATE OF MASSACHUSETTS. ONE ONLY HAS TO LOOK AT THE LIST OF WITNESSES FOR THESE HEARINGS AND YOU WILL SEE THE IMPACT WHICH OUR STATE HAS HAD ON THE ISSUE OF COMPETITIVENESS.

IT GIVES ME GREAT PLEASURE TO RECOGNIZE TWO WITNESSES WHO HAVE BEEN SO KIND AS TO APPEAR BEFORE THE COMMITTEE TODAY

MICHAEL CAMPBELL, PRESIDENT OF NOVA TECHNOLOGY IN GLOUCESTER, MA., WHICH IS IN MY DISTRICT, AND **JACK RENNIE**, PRESIDENT OF PACER SYSTEMS AND A VERY GOOD FRIEND OF MINE. IN ADDITION, I WOULD LIKE TO MENTION THAT **JOHN CICCARELLI**, DIRECTOR OF THE MASSACHUSETTS SBDC, WILL BE A WITNESS TOMORROW.

COMPANIES SUCH AS NOVA TECHNOLOGY AND PACER SYSTEMS REFLECT THE ECONOMIC RENAISSANCE WHICH HAS TAKEN PLACE IN THE COMMONWEALTH OF MASSACHUSETTS.

COMMUNITIES IN THE COMMONWEALTH WHICH HAD BEEN DEVASTATED BY THE DECLINE OF TRADITIONAL HEAVY MANUFACTURING ENTERPRISES HAVE TODAY BECOME CENTERS FOR THE INNOVATIVE USE OF NEW TECHNOLOGY, LEADING THE WAY FOR THE REST OF THE NATION IN TERMS OF NEW JOB CREATION, INNOVATION, AND COMPETITIVENESS.

MASSACHUSETTS HAS FOSTERED A STRATEGY WHICH ATTEMPTS TO MEET THE NEEDS OF ALL BUSINESSES BOTH SMALL AND LARGE, AND OF LABOR AND MANAGEMENT. A KEY TO THE MASSACHUSETTS SUCCESS STORY IS THAT IT HAS ENCOMPASSED A BROAD RANGE OF GROUPS AND IDEALS. THE ONLY QUALIFICATION FOR ADMISSION HAS BEEN A WILLINGNESS TO TRY NEW IDEAS - NEW IDEAS THAT WILL BE VITAL TO THE COMPETITIVENESS OF AMERICA IN THE INTERNATIONAL ARENA. IMPORTANTLY, THIS TRANSFORMATION HAS OCCURRED WITH A MINIMUM OF DISRUPTION. THIS HAS LARGELY BEEN ACHIEVED THROUGH PARTNERSHIP AND CONSENSUS BUILDING, THROUGH THE BELIEF THAT SOLUTIONS TO OUR

GREATEST PROBLEMS ARE POSSIBLE WHEN COOPERATION IS ACHIEVED. MASSACHUSETTS HAS LEARNED THE VALUABLE LESSON THAT IN THESE TIMES OF SCARCE PUBLIC RESOURCES, THOSE THAT ARE AVAILABLE MUST BE DIRECTED TOWARD HUMAN INITIATIVE, TO THOSE PEOPLE WHO WILL BE RESPONSIBLE FOR FOSTERING THE CLIMATE FOR INNOVATION IN THE UNITED STATES.

TRULY THE SUCCESS STORY OF THE MASSACHUSETTS ECONOMY IS A REMARKABLE ONE. I TRUST THAT THE REST OF THE NATION WILL SOON LEARN SOME VALUABLE LESSONS FROM OUR EXPERIENCE. THANK YOU.

PREPARED STATEMENT OF LIONEL H. OLMER, OF PAUL, WEISS, RIFKIND, WHARTON & GARRISON, AND FORMER UNDERSECRETARY OF COMMERCE FOR INTERNATIONAL TRADE, U.S. DEPARTMENT OF COMMERCE

Mr. Chairman, it is a pleasure to be here today, and I hope that I can contribute to the important debate you have sponsored in the search for ways to do more for a vital part of the U.S. economy. The problems which face small businesses in the international marketplace are often similar -- and sometimes identical -- to those faced by multinational corporations. Foreign producers competing with U.S. suppliers of goods and services employ the latest technologies, have access to affordable capital, often pay less for their labor resources, are more numerous in most industries than previously, and are usually more knowledgeable about the particular markets in which they are involved. Consequently, initiatives devised to assist U.S. exporters in general should benefit small business as well.

In some ways, small business should be better able to adapt to increasing competition from abroad. Because of greater flexibility and less bureaucracy, small business has the theoretical ability to change product design and production methods relatively faster than larger business enterprises, assisting them in carving out market niches, as in specialty steel and high-tech machine tools. In the services sector these same strengths should make possible rapid adjustment to customer needs and the tailoring or customization of service to fit particular needs. In other ways, however, small business has greater difficulty prospering in the face of growing foreign competition.

Unlike multinational corporations, small business usually cannot transfer assembly operations or juggle production capacity overseas to take advantage of foreign economic prospects, investment incentives and disincentives, and other international developments. Moreover, a large corporation with many divisions can more readily afford to absorb losses during cyclical downturns than can a single-product or service company.

For many years, the federal government -- and more recently state governments -- has sought ways of drawing on the strengths of U.S. small business and means of compensating for its weakness, in order to encourage expanded participation in international trade. I fear that although sound minds, stout hearts and usually sincere motivations have been applied, the efforts have not borne sufficient return. Although much assistance is already available for small business, additional action is needed to transform these existing programs into a fully-fledged support network for small business exports.

As a first step, current efforts by the Commerce Department to assist small business with export licensing problems should be expanded. A small additional Congressional appropriation (less than $1 million) could enable Commerce to transform its existing small business support staff into a rapid-response advisory team capable of solving some of small business' many problems with the complex export control regulations. Large corporations, especially those with Washington offices, possess the resources to tackle export licensing problems internally. But, small businesses located far from Washington are hobbled with the cost of hiring consultants to fill out extraordinarily complicated forms and to personally shepherd export license applications through the interagency process. (I understand that legislation has been introduced in the House to open up a West coast office of the Department of Commerce that would be capable of issuing export licenses; I strongly encourage this initiative.)

The export license "user-fee" proposed in the President's FY '88 budget may deter many small businesses from exporting merchandise requiring a license. Most small businesses that are just beginning to export must apply for individual validated licenses for each shipment, in lieu of "bulk" or "distribution" licenses which authorize multiple exports on the authority of the company only. For these small businesses, the current proposed user fee of $50.00 per application would quickly add up as each order is received and each license filed. I urge a re-thinking of the user-fee proposal, perhaps with exemptions built in to accommodate small business, new-to-export, firms.

To assist small businesses in developing overseas contacts, the Commerce Department ought to consider ways of offering greater encouragement to small businesses to participate in its overseas trade missions--perhaps even at reduced rates. I believe such trade missions are an excellent method by which companies can be introduced to prospective foreign customers. Unfortunately, the expense of participating (often $8,000-10,000 per person/per mission) is frequently beyond the means of small businesses these trade missions could greatly assist.

Enhanced promotional efforts are warranted for three currently under-utilized government programs designed to assist small business. The contact facilitation service operated by the Office of Export Trading Company Affairs at Commerce provides a useful means of bringing U.S. manufacturers in touch with experienced exporters. The Office of Trade Finance, also within the Commerce Department, assists small business exporters in obtaining corporate tax exemptions for that portion of earnings generated by certain export-related activities, as allowed by the Foreign Sales Corporation Act of 1984. Finally, the small business credit program, administered by the Export-Import Bank, is empowered to provide standby assurances to encourage U.S. commercial banks to extend fixed-rate, medium-term export loans to small business. All three of these programs are useful export-promoting vehicles that deserve additional attention and publicity; this would necessitate increased funding, in all likelihood.

On a separate front, to help small business afford essential technology and thereby improve its efficiency, tax-based capital investment incentives eliminated in the Tax Reform Act of 1986 could be reinstated. A redesigned investment tax credit and accelerated cost recovery system would serve this purpose, as would an increase in the tax credit allowed for research and development expenditures. These tax-based incentive programs could be reestablished with a sliding-scale of permissible deductions that would decrease the percentage allowances as a business's size increased.

Present efforts to promote the export performance of U.S. small business are laudable, but additional steps are justified. It has often been said, contrary to this view, that the vast majority of U.S. exports are accounted for by a relatively small handful of extremely large corporations and that government efforts to promote international trade should for the most part ignore small business. But the fact that there truly are tens of thousands of small and medium-sized companies across America which have the technical, managerial and product know-how to successfully compete anywhere, coupled with America's large and seemingly intractable trade deficit, should make it apparent that we can ill afford to ignore any prospectively helpful area of our economy. And if it takes a little more seed-money to energize this sector, it would seem to me to be a most worthwhile investment.

Thank you for this opportunity to testify.

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National Federation of
Independent Business

NFIB

STATEMENT OF

JOHN C. RENNIE, PRESIDENT/CEO
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for the

NATIONAL FEDERATION OF INDEPENDENT BUSINESS

Before: House Committee on Small Business
Subject: Trade Policy Reform Legislation
Date: March 24, 1987

Introduction

Mr. Chairman, I am pleased to testify today on behalf of the National Federation of Independent Business and the over half million members who belong to NFIB. We welcome this opportunity to comment on U.S. trade policy and small business.

I would like to compliment Chairman LaFalce for holding these hearings and for stepping out to secure a small business title in the House trade legislation. It is the first of what we hope and anticipate will be many opportunities for the Small Business Committee to assert the interests and importance of small business in debates not traditionally assigned to the jurisdiction of this Committee.

With the U.S. trade deficit reaching record levels in recent years, fear has escalated that the United States is losing its competitive edge in markets throughout the world. As imports increasingly penetrate our domestic market, the fear has spread to encompass concern about the ability of American companies to compete at home as well. As small business leads the nation in job creation and produces nearly 40% of our gross national product, it is a sector many policymakers are turning to in the search for solutions to overcome the imbalances in the U.S. economy, both domestically and abroad.

Certainly, we can offer some answers to the problems, given the prominent role of small business in our economy. But the expectations as to what small business can do to offset our trade deficit cannot be too high. The main market for most small firms is, and will likely continue to be, their own back yard. Ultimately, the Congress must deal with problems of our domestic budget deficit and continue to bring the dollar down to more realistic levels vis-a-vis other currencies in order to overcome the imbalances with our trading partners.

The small business interest in trade issues is twofold. First, some firms are interested in opportunities for exporting and competing abroad. These potential exporters, however, need better education and service as to how to go about exporting. Second, small business owners are obviously concerned with their ability to compete in the domestic market, and therefore they are concerned with the impact of import policies on the domestic economic front.

This testimony will set forth suggestions for developing policy which can best enhance the role of small business in international trade. Specifically, the testimony will focus on export promotion and the need for better small business representation in trade matters. Particular emphasis will be placed on the role the Small Business Administration (SBA) can play in these matters. We will also present the views of small business on the overall approach of trade policy and its impact on the domestic market.

Specifically NFIB supports measures promoting reciprocity, not protectionism. The testimony also notes support for efforts to strengthen the protection of intellectual property rights.

Export Promotion

Efforts to increase exporting by small firms are not new. Im 1980 Congress passed the Small Business Export Enhancement Act (P.L. 96-481), establishing a contract and grant program in the Department of Commerce for public and private entities which could counsel small firms on exporting. The Export Trading Company Act of 1982 (P.L. 97-290) allowed for the establishment of trading companies to handle all aspects of exporting for firms in a way which protects the participating financial and promotional parties from liabilities under the antitrust laws. The law allows for joint exporting ventures and for banking institutions to own a share of the venture. In 1984, the Foreign Sales Corporation (FSC) legislation, establishing tax incentives for exporters within the bounds of GATT, contained particular provisions to make FSCs workable for small firms. Other programs at the Department of Commerce, the ExIm Bank, and SBA have focused on promoting exporting by small businesses.

Despite these efforts, small firms continue to be largely uninterested in exporting. In February, 1985, NFIB's Research and Education Foundation published a study entitled "Small Business in Export Markets". The purpose of the study was to explore what contributions small business could make to bringing down U.S. trade deficits. The findings of the study include the following:

*Few small businesses export. Of those which do export, foreign sales usually account for less than 10% of total sales.

*Most small manufacturer/exporters engage in foreign trade infrequently. Nearly one in ten exporters have not made a foreign sale in three years.

*The initial export sale tends to be the product of an unsolicited order for a very small amount from a firm in an English speaking country. It is filled by the American firm very rapidly.

*The single most important motivation for a firm to enter the export market is an unsolicited order from abroad. Profit potential -- largely unrealized -- and the "the only way to expand" follow as motivating factors, though far behind unsolicited orders.

*The most important problem area for new exporters is obtaining market information. Foreign import restrictions are also cited frequently.

*The strong dollar is considered the greatest impediment to expanding export sales. Obtaining market information is also important.

*"Too much red tape," Better opportunities in USA," "Too complicated," "Too hard to find customers," and "Firm not big enough," are the principal reasons cited for not exporting.

*Government and private initiatives to increase small business exports should focus their efforts on: 1. firms with specific demographic characteristics, and 2. matching those firms, particularly for an initial export sale, with a foreign customer.

What more can be done to overcome these problems and encourage more small firms to export? Again, it must be acknowledged that some of the barriers to engaging more small firms in export activities will never be broken down. Small businesses are generally more comfortable in domestic markets, and the opportunities for growth in the domestic market are generally challenging enough. But, where programs exist to assist small business, there could be better targeting toward export promotion.

Perhaps the major problem for small firms that might be interested in exporting is a lack of knowldege of what help is currently available to them. Even if they are aware that assistance is available in the the trade area, locating the right program in the right agency to deal with their particular problem is enough to scare them away.

NFIB supports the concept of a Department of International Trade in order to consolidate the trade functions now scattered throughout a variety of federal agencies. The fifth recommendation of the 1986 White House Conference on Small Business calls for the creation of a cabinet-level department of international trade to "coordinate and focus on existing activities of federal agencies". The recommendation expressed the need to "Coordinate the dissemination of information regarding business opportunities, export financing, education and training, licensing, trade missions, market-driven data bases, SIC code updates, and other essential functions of international trade." Consolidating our trade functions into a single department is certainly beyond the scope of this committee, but we mention this point to emphasize the need for better coordination between the existing export and trade assistance programs. There needs to be more focus on matching the potential exporter with the program which can answer his or her needs.

A useful function for the trade offices at the Small Business Administration would be to serve as a facilitator and liaison between the small business interested in exporting and the other agencies with services to offer. To the extent possible, there needs to be a "one stop shop" for small firms interested in exporting.

Data from the NFIB study on small business and exporting indicate that if presented with an opportunity to fill an order abroad, most firms (75%) will try to fill them. Over 62% of the surveyed firms reported their first export sale was the result of an unsolicited order. The study also indicates that certain types of firms are more likely to export than others. In general, regular exporters tend to be firms with 20 or more employees. The majority manufacture more technologically advanced products, and they tend to have larger management teams. Programs designed to stimulate small business exporting should then be targeted toward those firms with the best potential for becoming regular exporters. To get these firms started, they need to be matched directly with customers or intermediaries.

Provisions in the major trade bills (H.R. 3 in the House, and S. 490 in the Senate) call for setting up centralized data banks at the Department of Commmerce. H.R. 3 also focuses on strengthening the Foreign Commercial Service by directing resources at our embassies abroad to promote U.S. business interests and to gather market information. This type of information could be disseminated through a central data center. SBA could help potential exporters by directing them to these resources.

Better incentives for exporters, and better education on what incentives exist, needs to be explored as well. Export trading companies are effective in that they offer the needed intermediary assistance through the private sector. The NFIB study shows that a majority of exporters have at one time or another engaged an export intermediary. Here again, though, there is a problem of matching the intermediaries with the potential exporters.

The tax incentives provided by the Foreign Sales Corporation (FSC) are worthwhile. We would encourage examination of the FSC to see if these tax incentives might be enhanced for small exporters. In addition, there needs to be a review of the "Small FSC" structure to determine if it can be simplified further to meet the needs of small firms. NFIB also supports using these types of incentives to encourage service exports as well as product exports. Again, SBA can serve a role by educating potential exporters on incentives like the FSC.

Another incentive proposed by the White House Conference on Small Business is the creation of an "Export SBIR". Such a program would operate along the lines of the Small Business Innovation and Research program by awarding grants to small firms with the potential for exporting and promoting growth in exports. As with the SBIR program, funds for the "Export SBIR" should be set aside from other existing programs. NFIB supports the concept of the "Export SBIR", and we commend Congressman Norman Sisisky for beginning to explore development of such a program.

The Small Business Administration can play a more significant role in the trade area through enhancing its education services, serving as a facilitator between small firms and other agencies, and perhaps through promotion of incentives such as the "Export SBIR", but implementing these ideas must be looked at in the context of the SBA and its programs as a whole. As with any problem we face on a national scale, there is a tendency to want to just throw more money at the problem to make it go away. Particularly in the trade area, this will not work. As we have already noted, the need to bring down federal spending is an important element in solving our trade problems. We would thus encourage the Committee to look at the budgeting for new programs such as the "Export SBIR" in the context of allocating SBA's resources overall.

In addition to careful consideration of budget allocations, NFIB asks the Committee to think carefully about its approach to using SBA programs in getting information to potential exporters. NFIB has testified many times before this Committee on the role of the Small Business Development Centers (SBDCs) and the need for improving Management Assistance programs at SBA. If these programs are to be used in the export promotion efforts, we encourage you to focus on the most effective elements in these programs. A survey of NFIB members indicate they trust most the advice given them by retired business owners and private consultants. College professors and university business administration teachers are the least trusted sources of advice. Where possible, we urge the Committee to use the private sector for information dissemination and technology transfer. A role for the SBA could again be that of facilitator connecting the private consultant and the potential exporter.

Increased Small Business Representation in Trade Matters

Another major problem of small business in the trade area is lack of focus on the small business perspective on trade. NFIB has proposed increased representation of small business in trade matters through the establishment of a Small Business Advocate in the office of the U.S. Trade Representative (USTR) or by designating an

Assistant Secretary for Small Business and Trade at Commerce. The White House Conference on Small Business recommendation on trade also called for increased representation of small business in trade matters.

H.R. 3 addresses this concern to some extent (thanks to provisions sponsored in last year's debate by Congressman Bill Archer. Where the bill establishes councils or committees to address trade issues, it specifies that representatives of small firms shall be included as members. For example, where industry adjustment plans are developed for industries injured by imports, advisory councils are set up to establish the industry plan. The bill specifies that 2 to 4 members of the council shall be representatives of firms within the industry, one of which shall be a representative of small business. The bill also establishes a Council on Industrial Competitiveness, which is to include small business representatives as members.

H.R. 3 also moves toward establishment of a Trade Advocate for Small Business. The bill, as introduced, established in the USTR's Office a Fair Trade Advocates Branch to assist "qualifying industries in obtaining remedies and benefits under the trade laws". The definition for "qualifying industry" includes any small business which, due to its size, does not have the resources or financial ability to obtain legal and technical assistance. Unfortunately, these provisions were pared down somewhat in the full Ways and Means Committee mark-up of the bill. The marked-up bill would establish a Trade Remedy Assistance Office at the International Trade Commission (ITC) to provide information to the public and advice on remedies and petition procedures. Less focus is put on assistance to small business in this version.

The advocacy role of SBA could also be used in this area. The legal and technical resources of small businesses are often limited. SBA could assist small firms in preparing for and participating in proceedings relating to trade laws. The advocate's office could provide assistance to small business with filling out forms, filing petitions, and post-petition proceedings. Of course, functions should be coordinated with the structure of the proposed Trade Assistance Office at ITC. But maybe a role for SBA in serving to offer assistance to small firms exclusively in trade remedy cases. Again, however, we reiterate the point that this would drain resources from the existing programs at SBA, including current functions within the Office of Advocacy itself.

NFIB also supports efforts to expedite procedures in trade injury cases where "critical circumstances" exist. Swift action can be particularly important in the case of small firms which operate close to the margin.

Impact of Trade Policy on the Domestic Market

Small business owner's interest in trade matters also stems from their concern over the impact of imports and overall trade policy on the domestic U.S. market. Their view in this area is primarily that of the free trader. How can we maintain the competitive stance of domestic producers against that of imports from abroad? The answer, in the view of members of NFIB, is to promote the abilities of small firms to compete by providing an atmosphere for business operations which is relatively free from government regulations and mandates. The answer, in the opinion of NFIB, is not to close our markets to competition from abroad, but to enhance the opportunities for American goods and services to compete with imports from abroad.

Other committees are dealing with trade remedies and the procedures for negotiating agreements with our trading partners. We include comments in this testimony on some of the approaches being considered by other committees in the event that Small Business

Committee members have an opportunity to deal with these issues in their role as members of other committees or in discussions with members of those committees.

NFIB opposes rigid protectionist approaches to addressing our trade problems. Particular provisions in H.R. 3, the major trade bill in the House, raise concerns. These include the "Gephardt" provisions which are directed against countries running "excessive" and "unwarranted" trade surpluses with the U.S. The President must, under these provisions, attempt to negotiate defined surplus reductions. If negotiatons fail, the President must take further action to achieve reduction goals. This action includes suspension of trade agreement benefits and the assessment of duties and import restrictions as the President deems appropriate.

NFIB members have opposed proposals restricting imports of goods from abroad. A 1981 Mandate survey showed 68% opposed to limiting imports of foreign-made automobiles. A 1982 Mandate survey showed 57% opposed to domestic content proposals. In 1985 56% opposed voluntary import quotas on automobiles. The required percentage reduction of surpluses and the inflexible imposition of duties or quotas on imported goods are tools of retribution against our trading partners. The goals should be that of reciprocity, more open markets, and the lowering of trade barriers. These provisions have been modified in the mark-up process to give the Administration more discretion in taking action against surplus countries. The modifications make these provisions less objectionable, and we would hope that the more moderate provisions will be retained.

NFIB also objects to the proposals to define as "unreasonable" practices that deny internationally-recognized worker rights (right of association, right to organize and bargain, prohibitions on forced labor, minimum employment age, minimum wages, hours of work, and occupational safety and health). These provisions essentially impose U.S. labor standards on foreign countries. Companies operating abroad should not be expected to abide by the standards set by the U.S. government.

Other provisions in H.R. 3 pose potential problems for small firms. These provisions would allow a U.S. manufacturer, producer, or wholesaler of a product who is injured economically by the dumping of imports to bring suit against a manufacturer, exporter, or importer "who knew or had reason to know that the merchandise was sold at less than fair market value." The injured party may recover actual damages. Under these provisions, the small retailer or wholesaler who sells imported goods could be open to suit.

Although the knowledge standard may be difficult to prove, the opportunity for suit can only add to the litigation explosion in this country and to the resulting problems of liability insurance coverage.

Discretionary Executive Actions and Reciprocity

While NFIB opposes specific protectionist measures in H.R. 3, certain moves to eliminate the discretion of the President to act in unfair trade cases can be supported. These provisions will promote reciprocity as the guiding force behind our trade policies. NFIB Mandate polls show small business owners supporting by 61% a policy of strict reciprocity in trade with foreign countries (1982 Mandate). Under H.R. 3, and the major Senate trade bill, S. 490 (sponsored by Finance Committee Chairman Lloyd Bentsen (D-TX)), the U.S. Trade Representative (USTR) is given greater authority to initiate investigations into unfair trade practices (Sec. 301 cases), and upon certain findings, the President is required to attempt to negotiate elimination of the unfair trade practices.

H.R. 3 mandates that the President take action against countries engaging in unfair trade practices, that is, countries acting inconsistently with, or violating, U.S. rights under trade agreements. S. 490 would also mandate the President to retaliate in the case of unfair trade practices. The extent to which the President was directed to act in the Gephardt provisions originally in H.R. 3 was of concern to NFIB for the reasons noted above. But mandating some action (with the President given discretion as to what that action will be) is consistent with a policy of reciprocity. The modifications made to H.R. 3 by the Ways and Means Committee, however, seem to answer our concerns.

Provisions dealing with Section 201 cases to provide relief for industries injured by import dumping also limit the President's discretion to act. Both bills would turn more authority over to the USTR and the International Trade Commission (ITC) to determine when action is necessary to address an injury. Under S. 490, if the ITC voted unanimously in favor of retaliatory action, the President would have to act unless he offered an alternative plan which was accepted by Congress. Review of alternatives would be on an expedited track. H.R. 3 gives the USTR the authority to act in import relief cases.

In import injury cases, an industry or company petitioning for relief will often go through a long, time-consuming procedure to prove its case for relief. Once the ITC makes a determination that relief is warranted, the USTR must concur and then recommend to the President that action be taken. Often at this point, the State Department or other agencies involved in foreign affairs will come forward with political reasons unrelated to trade as to why action should not be taken. Giving the USTR greater authority and limiting the President's discretion in these cases will assure that industry and trade interests, and not unrelated political interests, govern whether action is taken in these cases. These provisions further promote the goal of strict reciprocity.

Protection of Intellectual Property Rights

NFIB supports provisions contained in all of the major bills to strengthen laws protecting intellectual property rights. We encourage the Small Business Committee to lend support to these proposals as well. These provisions would prevent imports of products which infringe on active patents, trademarks, and copyrights in the U.S. The bills would also make protection of intellectual property a topic for the GATT talks and would also call for negotiations on lowering market barriers, such as licensing and fees requirements, in other countries. Such provisions were supported in the White House Conference on Small Business recommendations. (See recommendation #5 and #15.)

Conclusion

NFIB once again would like to commend the Small Business Committee for playing an active role in the trade debate. In summary, we urge the Committee to focus its efforts in this debate on:

--Establishing a more defined role for SBA as a source for information on exporting and as a facilitator for linking potential small exporters with trade assistance programs;

--Promoting improved and new incentives for small business exporters;

--Providing better representation for small business in trade matters;

--Speaking for small business on the impact of our overall trade policy on the domestic market, particularly calling for reciprocity and not protectionist approaches, and calling for better protection of intellectual property rights.

The contribution which small business can make in the trade area will depend on policies which recognize the abilities of small firms as well as the limitations and special needs of small firms. We appreciate this opportunity to present the views of NFIB as to how those policies can best be framed.

TRADE AND COMPETITIVENESS ISSUES

WEDNESDAY, MARCH 25, 1987

House of Representatives,
Committee on Small Business,
Washington, DC.

The subcommittee met, pursuant to notice, at 1:10 p.m., in room 2359-A, Rayburn House Office Building, Hon. John J. LaFalce (chairman of the committee) presiding.

Present. Chairman LaFalce; Representatives Luken, Skelton, Mazzoli, Sisisky, Olin, Bilbray, Flake, Lancaster, Price, McDade, Ireland, Slaughter, Gallo, and Rhodes.

Chairman LaFalce. The Committee on Small Business will come to order.

Today, we are holding the final hearing in a series of general hearings this committee has been conducting on competitive problems and opportunities facing our small business sector.

Next week, our Small Business Committee will consider legislation for inclusion in the House Omnibus Trade Bill to deal with these important issues.

Up to this point, there has been a serious gap in the trade debate, an important sector of the economy whose problems have been virtually ignored. Our small- and mid-sized companies are key sources of economic growth and investment. Yet, their unique concerns have remained largely unaddressed, as the concerns of our larger corporations have driven the trade debate.

Small- and mid-sized companies account for half of our private work force, produce half of our gross domestic product, and have created nearly two-thirds of the new jobs of the last decade. These companies are the driving forces behind many of our advances in technology. Three-quarters of America's great corporations rely on small firms as suppliers, manufacturers, distributors, and customers. Entrepreneurs have spawned new businesses, indeed, whole industries, while bigger firms have all too often been mired in outdated business practices.

But the potential of small- and mid-sized companies to contribute to the growth of the American economy and the overall international competitiveness of the United States is increasingly at risk. To date, public policy has done little to help. It is now time to look forward and take positive steps to provide the environment in which the U.S. companies can flourish; to rethink the potential of entrepreneurs and small- and mid-sized companies as forces for economic growth; and to help provide the competitive environment in which that growth can occur.

We must make competitiveness the linchpin of our economic policy. To do so, we must expand export opportunities; assist smaller U.S. firms in their efforts to combat unfair foreign competition in the domestic market; minimize impediments to the growth of smaller innovative firms; facilitate technology transfer; increase access to long-term capital; and, generally, create the conditions that foster innovation and business development.

We have much to learn from those working on these issues at the State and local level, in some cases under the auspices of the Small Business Development Center Program. For example, the State of Alabama puts out export promotion material in several languages, including Chinese and Japanese, and does aggressive marketing on behalf of its smaller firms.

Florida is attempting to expand trade opportunities for small businesses through the State SBDC, which is operating as the State International Trade Center. Massachusetts is working to institute quality control procedures in smaller manufacturing firms that will make them more viable both as subcontractors and independent competitors. Pennsylvania is working hard on technology transfer. Missouri is assisting smaller manufacturing companies hit by import competition to change their production and marketing strategies.

But the States cannot bear the burden alone. If we are to have the export-led growth necessary to turn our trade deficit around, the Federal Government must play a stronger catalytic role.

Today, we are pleased to have with us the Honorable Andy Ireland, ranking minority Member of the Subcommittee on Exports, Tourism, and Special Problems. We also have representatives from the Small Business Development Centers—Susan Garber, Pennsylvania State Director; John Ciccarelli, Massachusetts State Director; Greg Higgins, Florida State Director; and Fred Hale, Missouri State Director. From the National Tooling and Machining Association, we will hear from Daniel Bailey, President of Rochester Gear, Inc., who also happens to be a constituent of mine, and a fellow graduate of the Jesuit University; Mary A. Wathen, president of Koboway, Inc., on behalf of the American Electronics Association; and the Honorable Leanna Brown, State Senator from the State of New Jersey.

Before we begin, does any member of the full committee have any comment they wish to make? [No response.]

Before we begin, I am going to have to make my apologies. We deliberately scheduled this hearing for the afternoon because the Banking Committee had scheduled a markup session on its title of the trade bill for this morning, and then they switched their markup session to this afternoon. Since I am the principal author of each of the banking provisions within the Banking Committee's title, I am going to have to go there to defend those bills, and I am going to ask the chairman of the Export Subcommittee of the Full Small Business Committee, Representative Skelton, if he would now assume the chair and conduct the full committee hearing.

Thank you.

Mr. SKELTON [presiding]. Thank you.

We are pleased to hear from our colleague and friend, Mr. Ireland.

Mr. IRELAND. Thank you, Mr. Chairman.

I would remind you, Mr. Chairman, that you and I have worked hard for some 10 years to direct peoples' attention toward the trade problem and the very important part that the small business community does and will play in the whole trade area. We are at a crossroads right now in trade as I think we all realize, and the road to success will likely be led by small business.

I would like to commend the chairman for securing a separate title for small business in the upcoming legislation, and I must say that I have mixed emotions about the jurisdictional problem that confines the title we have under consideration to the activities of the Small Business Administration. I believe that our committee has a responsibility to call the needs of the small business community to the attention of other committees of this House. So, if I am allowed, I would like to first discuss the SBA and its relationship through its title to the trade legislation and then offer some suggestions which will certainly loom outside our technical jurisdiction but which I feel deserve our attention as legislative advocates of the small business sector of the economy.

The record is very clear. At the present time, no one and I emphasize that, no one speaks for small business in the upper echelons of Federal trade policy. Therefore, now may be the ideal time to make the Small Business Administrator slot a cabinet-level position. To do this actually requires a minimal, roughly $5,000 increase in pay for the Administrator.

There is no legal problem involved because the Cabinet exists by tradition and not by law, and I would also doubt that in pushing for the cabinet-level position for the Administrator that we would have any jurisdictional disputes raised by other committees.

If we are able to accomplish this at this time, we would have solved one major problem and that is we would have created a voice for small business at the crucial upper echelons of trade meetings.

Next, I would suggest that we replace the current director of international trade slot in the SBA with a new agency slot entitled Assistant Administrator for Trade. This individual would then oversee the current office and also would assume any new duties added by the various proposals and there are some good ones, various proposals we are now considering here in this committee.

In addition, a part of this new individual's duty should be some form of permanent working relationship with the State and local governments in their efforts in the trade area. Anyone who has even casually studied the trade issue knows that the most innovative and constructive efforts in the expansion of exports has come from State and local governments.

You might be interested to know, for example, that at the present time, our 50 States now spend more money annually on export promotion than does the entire U.S. and Foreign Commercial Service of the Department of Commerce. We could do worse as a committee than to direct SBA's energy and resources to helping these already successful programs.

Those are my thoughts, I think, for the things that we can do within the SBA and, indeed, they are limited, but I would like to share with you and the other members of the committee, Mr.

Chairman, some other thoughts that I have developed over recent years which I believe will bring about a greater participation by small business in export markets.

I agree with so many who have pointed out and as the chairman did before he left, that small business is the key to the return of American competitiveness worldwide. I certainly do not claim that the following list of proposals is complete, nor that as it stands it does not need some modifications, nor that it does not touch on the areas of responsibility of our fellow committees.

However, I believe that as a committee, we have a responsibility for what might be called legislative advocacy similar in our domain here in Congress to the SBA's chief counsel for advocacy in his role to support small business in the executive branch.

I would suggest that we address these initiatives on behalf of small business by perhaps calling our colleagues' attention to their importance in the form of floor amendments or in the record of floor debate on the final trade bill.

My suggestions would be as follows: There should be appointed a small business assistant trade representative within the U.S. Trade Representative's office. At the present time, there are more than 44 assistants, none of whom deal with small business. It is appalling for this Nation not to have a voice at the GATT round, for instance, that speaks for small business.

This last September, the American group left for Uruguay for the beginning of the GATT round. A small business representative was allocated one seat on the plane and at the last moment he was bumped. That is the level of support that the small business community has in our trade talks right now. In contrast to that, as I think we well know and have heard in testimony over and over again over the years, that despite the feeling that our difficulties with Japan are with Toyota and Nissan, in actuality, the bulk of imports to the United States from Japan come from small Japanese businesses.

So, there is no question that we should have a bigger input at the U.S. Trade Representative's office.

Second, all United States ambassadors should be required to provide a brief annual report to the Secretary of State and to the Congress on their export promotion accomplishments relative to small business as well as any innovative programs that they find in the countries that they are domiciled that those countries do for small business.

Now, admittedly, to most of the folks in the Foreign Service, in order to make that report, you will have to introduce them to what a small business is or maybe what a business is, but certainly we deserve, if we are going to be supporting people in embassies around the world, to have people speaking out for American business of all sizes and at the same time reporting back to us what is going on.

Third, I think there are some things that the U.S. Department of Commerce should be required to do that could certainly help small business. The first of these is to conduct a biennial meeting in the form of a national trade, national conference, featuring small business trade and economic development from the Secretaries of Commerce of the fifty states, the District of Columbia, and the U.S. Territories.

I think very obviously what we found out is that the real action is going on in the states and the Department of Commerce could do well to bring these people together, support them and learn a little something from their activities.

The Department of Commerce should undertake a study of the effects on U.S. international competitiveness of state tax systems, including their effect on small business trade promotion, the utilization of FISCS, the small business capital formation for small business.

The Commerce Department also should instruct the Bureau of Analysis to produce a gross state product figure for all States the District of Columbia, and the U.S. Territories. In doing this, such figures would certainly further enhance the successful export efforts of the many fine state and local programs. Right now, the Department of Commerce cannot furnish the kind of figures that the state and local programs can use to demonstrate and target their efforts.

Certainly the Department of Commerce should join in a small business policy and export promotion advisory commission along with the SBA, the U.S. Department of Agriculture, and the Special Trade Representatives Office. Such a commission would coordinate on behalf of small business the efforts of each one of those agencies.

The Department of Commerce should be required to increase the term of membership in all industry sector advisory committees from 2 to 4 years. It is a sad tale when you realize that some fifteen of those vacancies have been unfilled for almost seven years and in that 7 years that the small and minority business ISAC has never been blessed by the attendance of the Secretary of Commerce, even on one occasion.

The Department of Commerce should, in my judgment, do a study to determine the feasibility of merging or co-locating the district offices of U.S. and Foreign Commercial Service with existing State export promotion offices. Obviously, the convenience of the small business community would be greatly served by having all this activity in a central location.

The Department of Commerce should cause a study to be done with an eye toward overhauling of the Standard Industrial Classification, the SIC code, to determine what industries are currently being overlooked. As testimony before this committee has already shown, many service industries are not even accounted for under our SIC codes, which leads even one major economist to wonder if we even have a trade deficit since we are not counting an awful lot of what we are doing.

Also, both export trading companies and export management companies should have their own SIC codes since otherwise there is no way that we can figure out from their statistics what their activity has been.

The Economic Development Administration should be required to set aside $100,000 a year for each State for the purpose of encouraging State strategic small business economic trade plans. After all, this is where the action is, the EDA spends a substantial amount of money every year. Certainly this small amount of money would enhance the one area that we know is successful.

The Eximbank and the SBA should consult and report to Congress within 6 months on a plan to develop risk protection plans for State small business export financing programs with a minimum of 80 percent coverage. The Eximbank has only put its toe, so to speak, in the water of helping the small businesses of America and they have got a long way to go.

The President's science advisor should be compelled to have a coordinator of Federal labs who would serve as a liaison with small business technology initiatives at the State level. Obviously, this is an area where we can compete, should compete, and we should help small business in any way we can.

Mr. Chairman, I believe that each of these activities is something that is achievable through the work of this committee and that with this committee's activity and interest, we can really do something in this Congress for small business in the area of trade.

Thank you.

Mr. SKELTON. Mr. Ireland, I thank you so much.

You mentioned many years of interest in this area, and your recommendations are excellent. Hopefully, they will be successful.

I know what you mean when you say no one speaks for small business in the upper echelons of trade policies. No one is there. It is just a complete vacancy.

Let me ask you this question, if I may. Are there some of your recommendations here that can come through this committee without getting into the jurisdiction of one of the other committees in Congress?

Mr. IRELAND. Well, I think the two that address this title, one, elevating the Administrator.

Mr. SKELTON. The first two you mentioned.

Mr. IRELAND. The first two certainly can.

I would point out that raising the status of the Administrator is one high on the list of the White House Conference recommendations. Contrary to the detractors of that idea, it does not create additional bureaucracy. It merely takes the person that represents that part of the economy—as the chairman said in his opening remarks, 50 percent of the gross national product of our economy and most of the new jobs—and puts him in the highest policy councils in our Government.

In giving him that status, most certainly over the years to come, it will attract more high-caliber people being interested in serving in that position. So, I think those are things that can have a substantial amount of impact without going to other committees.

Mr. SKELTON. Thank you.

Mr. Gallo.

Mr. GALLO. No questions.

Mr. SKELTON. Any questions?

[No response.]

If not, we certainly thank you again, sir.

Mr. IRELAND. Thank you.

Mr. SKELTON. Before I ask the remainder of the witnesses today to serve as a panel as was suggested earlier, John Ciccarelli, Greg

Higgins, Susan Garber, Fred Hale from my home State, Dan Bailey, Jim McManyon, and the Honorable Leanna Brown.

It seems like all of us during the hearing season, as we call it, Senator, you know what I mean, we find ourselves having to be in two places at one time. I turn into a pumpkin at two o'clock and I understand there will be someone taking this Chair at that time.

I will recognize first the gentleman from the State of Missouri, Mr. Fred Hale, State Director of the Small Business Development Center.

TESTIMONY OF FRED HALE, STATE DIRECTOR, SMALL BUSINESS DEVELOPMENT CENTER, ST. LOUIS, MO

Mr. HALE. Thank you, Mr. Chairman.

It is a privilege for me to be here and share with you all today some of the things that are going on in Missouri that I think have application to the trade issue.

First off, I would like to give a very brief introduction to the Missouri SBDC Program. We are headquartered at St. Louis University, a Jesuit school in St. Louis. We operate 18 centers around the State.

Mr. SKELTON. That is not the Jesuit school that we were hearing about earlier, was it, Mr. Bailey?

Mr. BAILEY. I am afraid not.

Mr. SKELTON. All right. Go ahead, sir.

Mr. HALE. Of those, 15 are in institutions of higher education and we operate 1 center in cosponsorship with the State of Missouri.

Last year, our program provided counseling help to more than 2,200 small businesses, and part of what I am going to talk about today is the result of the exposure and visibility that we have had with those small businesses.

In response to one of the needs of Missouri small businesses, we have created—it is operating this year—a new small business development center that we call the Technology Development Center, and I will spend a few moments talking about that as well as a new program that we were fortunate to undertake just recently. We operate the Mid-America Trade Adjustment Assistance Center, funded through the Department of Commerce, as well.

First, I would like to, Mr. Chairman, talk about the Technology Development Center and the need that we saw in creating that center. Small businesses in Missouri, and I gather elsewhere around the country, are faced somewhat with a problem that I have called a technology application gap. As we are all aware, we have technology in this country in great quantities and in rather sophisticated areas.

The problem that affects small business is not that technology does not exist, it is in the application of that technology to the business problems and issues facing those small businesses. High technology that we all hear about and is talked about is a mystery to the typical small business person.

A good example in a recent application in our State, small business, when they hear the term robotics, instantly in most cases, think of the multi-million dollar pieces of equipment that they see at General Motors and Ford and the other auto producers. They do not think about the $1,000 off the shelf pick and place robot that properly applied can have a significant impact on the production in a very small, small business.

Another area that we see mystification, if you will, is in the area of materials. Many, many small businesses are operating as they have for years. They consider themselves a metal working company. Today, there are new materials in the areas of plastics and polymers that have many of the properties of metals and properly applied can increase that firm's capability and competitive edge in the marketplace. Again, those companies hesitate to think about plastics as a material.

Another area of substantial concern is that of small computers. A customized application of small computers in both production and process control is—we have just begun to scratch the surface. That is an area that could have far-reaching implications to the success of small business.

Well, given that background in Missouri, we created the Technology Development Center. This program is headquartered at Central Missouri State in Warrensburg, MO, and the purpose of this center is to assist Missouri businesses. This is a statewide program, to assist Missouri businesses in the application of existing technology or in the transfer of existing technology.

Our goal with this particular center is to take a no-technology company and convert it to a low-technology company, and in that conversion make that company far more competitive than it is at present.

This program is off to a roaring start. It services all the other 17 SBDC's around the State, and if reaction of small business in Missouri can be used as a measure at this point, this is going to be a roaring success. That center, just getting started, has more clients than it can sensibly handle at this point. We are already stripped of our resources before we even get this program up and running.

The second area that I would like to mention is one that I am very proud of, as is my school, and this is the movement of the Mid-America Trade Adjustment Assistance Center that has been dormant for more than a year to St. Louis University.

This is a program that operates out of the International Trade Administration of the Department of Commerce. It was created in the Trade Act of 1974. We are operating this program in a six-State region, and it provides direct assistance to manufacturers and processors who have been hurt by the competitive influence of imported products.

Manufacturers throughout the Midwest, and I am sure in other parts of the country as well, are faced with this problem on a regular basis. This program allows the resources of the Federal Government and, in turn, the contract resources of the private sector to address specific corrective action or adjustment plans in these small manufacturing concerns.

This program, when it was created, did not, as I recollect, have a small business title to it. It did not have a small business name. In fact, in the Mid-America Trade Adjustment Assistance Center, virtually all the clients we deal with are, in fact, small business. So, there is a small business program that is working and it is functional.

The innovation that we think we have come up with is the one that I have been asked to mention today—the marrying of the Trade Adjustment Assistance Program with the SBDC network. For example, in the Mid-America TAAC covering the six States, Missouri, Kansas, Arkansas, Oklahoma, Louisiana, and Texas, that region was covered in the past by one center located in that University of Arkansas, Little Rock.

When we took the program over several months ago, we are operating that program through the existing SBDC network in those six States. So, our outreach operating the Trade Adjustment Assistance Center, we have more than 50 outlets, 50 centers in those six States from which small businesses can learn of the characteristics and advantages of this program and from which we can do intake into the Trade Adjustment Assistance Center.

So far, that is working very, very well, I am pleased to say. We have gained efficiencies in the operation, not only in the administration and control of the program, but most importantly we have created some efficiencies in getting the word of this very, very good program into the hands of more small businesses throughout the region.

It works well for all of us. The Trade Adjustment Assistance Center Program gets more good businesses to work with, and the SBDC's within those six States get another program to help fill out those programs that we have available to deliver to assist small businesses.

My conclusions from the experience that we have had in Missouri is that small business needs more work in the area of applied technology and technology transfer. Those applications, properly done, can make small businesses more competitive, not only in the domestic marketplace but abroad.

The second conclusion that I have come to is that the existing SBDC network, in my case referencing the six States, that existing network provides a highly efficient and very quick program or vehicle to get information and programs into the hands of the small businesses throughout our States and, in this case, the six-State region.

Thank you again for the opportunity to be here, Mr. Chairman. I appreciate it and would answer any questions later.

[Mr. Hale's prepared statement may be found in the appendix.]

Mr. SKELTON. Thank you so much, Mr. Hale.

We will withhold the questions until the entire panel has testified, but special thanks for you coming from the great State of Missouri.

Senator Brown.

TESTIMONY OF HON. LEANNA BROWN, STATE SENATOR, STATE OF NEW JERSEY

Ms. BROWN. Thank you very much, Mr. Chairman.

I am indebted to my representative, Dean Gallo, and his staff for arranging this meeting here today. I am playing hooky from the budget process in the great State of New Jersey and, therefore, will not be able to stay till the end of these events here today.

I come from a little bit different perspective than some of your witnesses this afternoon because as a person who is involved in the New Jersey Commission on International Trade and involved with Representative Gallo's task force on small business export opportunity, I look at the trade imbalance as one of the hidden crises facing this Nation at this moment in time, and for too much of our history we have been able as United States citizens to see economic opportunities within our own borders.

In November, I took an interesting trip with my husband to the Far East. It was our third such trip, and I was very much concerned in talking to business and government officials in Tokyo and Seoul and Singapore and in Delhi about the lack of presence of American business in that part of the world.

So, I want to congratulate the committee today for showcasing a moment in time with the importance of trade because we have no greater challenge here in the United States than to build a constituency for international trade, and I think it is very interesting that small business is really leading the way, is looking for new opportunities and, as you all know, of course, the growth in American business since World War II has come from small business. So, maybe some of the representatives from larger corporations will get some good ideas from what your committee is doing.

Not only by having these hearings here today are you building a constituency for international trade, I also want to plug for a key role for the States. I am proud of New Jersey. We are No. 4 as far as the amount of reverse investment that is going on in our State and we are tapping the amount of exports that we do.

We have an excellent division on international trade and our Governor last year, like many other Governors, took the personal approach to getting business abroad and went to Seoul and to the Peoples Republic of China.

Third, I think we need to focus the Federal effort and a couple of specific suggestions which may or may not come within the jurisdiction of this committee, but I think just the fact that this committee is interested in having small business and trade linked closely, I advocate, in the specific way to make this possible.

In the general scheme of things, I would just like to say that even though in the State of New Jersey, when they talk about having new departments, I am relatively conservative. I would like to just verbalize that if we are looking at trade as a real key crisis here in the United States, I think it is reasonable to expect to establish a department of trade and have it have full-fledged Cabinet status.

Second, obviously, the improvement of all sorts of information about trade is vital to small business. I support the improvement of the export hotline and also I think it is a role of the Federal Government to get information into the hands of the State as far as who is doing what in the very vital business of exporting.

It was interesting to be in Seoul and right by the nightstand in the hotel room, of course, is a list of all the products that are exported from Korea. So, we have a long way to go in just making the basic information available to small as well as large business.

Obviously, we can upgrade our trade show operations. We can prepare small businesses more before they go on trade shows and also when they come back. We all know that in order to do business internationally, it takes patience and persistence and that instant millionaires are not made overnight but all of us need to take a look at our long-range business plan and be part of the international effort.

Again, international property right protection is key. There is no point in having a new invention at one of your centers in Missouri and to have that pirated by some entrepreneur in Taiwan. So, I think the window of opportunity for solutions for this old chestnut of intellectual property right protection has been opened by the President's bill, 1155, and, hopefully, some progress on this age-old problem can be made.

Last, of course, is the importance of cutting redtape and removing disincentives and trying to stream line the whole process of export licensing and not making life more difficult for small business people than is absolutely necessary.

So, again, bravo to this committee for helping to build a constituency for international trade and we at the State levels stand willing to help not only with dollars but with people to make things better for small business and the Nation at large as far as the whole trade picture.

[Ms. Brown's prepared statement may be found in the appendix.]

Mr. SKELTON. Senator Brown, thank you.

I have an announcement. Mary Wathen, the president of Koboway, Inc., Costa Mesa, CA, representing the American Electronics Association, was not on my first list. I did not call your name. I apologize.

Mr. Bailey.

TESTIMONY OF DANIEL BAILEY, PRESIDENT, ROCHESTER GEAR, INC., ROCHESTER, NY, ON BEHALF OF NATIONAL TOOLING & MACHINING ASSOCIATION

Mr. BAILEY. Thank you, Mr. Chairman and members of the committee.

My name is Dan Bailey, and I am president of Rochester Gear, Inc., in Rochester, NY. Our company and the estimated 12,000 other small manufacturing companies in our industry form the foundation of the United States' industrial base. Our highly skilled workers produce molds, dies, precision machined parts, special machines, and other tooling essential to modern mass production.

Our member companies are typically small, around 15 to 20 employees. We share characteristics with other manufacturing industries dominated by small businesses. We are internationally competitive. We accept this competition as healthy for our industry, making us stronger and more efficient, but just about every small manufacturer in this country has abruptly found his company undercut by predatory pricing by his foreign competitors in the last few years.

Virtually all small U.S. manufacturers are now being injured by unfair foreign competition and there is nothing we can do about it. The cost of bringing a case before the International Trade Commission can easily exceed several hundreds of thousands of dollars, more than the liquidated value of many of our companies. At the same time, it is a no-lose situation for the foreign competitor. They may not even get caught, and if they do get caught, they can still avoid the fine by ceasing to dump the product. In some cases, the penalty is so small of a fine that even that is not a deterrent.

At the same time, we find the U.S. Government encouraging this process. Federal procurement practices are currently exempted from commercial trade law. This has allowed several agencies, in particular the Department of Defense, to knowingly purchase foreign sourced products at prices that are generally below market levels. Yet, the U.S. manufacturer has no recourse.

There are two types of small U.S. manufacturers. The very small manufacturer is powerless. The net worth of the company is not enough to fund the necessary legal action. The larger of the small manufacturers might be able to borrow the money necessary to pursue the case but the costs would find their way back into increased product price, regardless of the outcome of the case, effectively closing off the litigation option for these manufacturers.

We have several specific recommendations for your consideration.

First, we suggest that a small business trade law advocacy program be established within the SBA Office of Advocacy. That program would assist small businesses by determining the degree of impact and whether foreign practices illegal under the GATT have taken place. Where both injury and unfair foreign competition has occurred, the SBA would be required to aid in obtaining the appropriate remedy.

Second, we suggest that Congress strengthen the private right of action provision for unfair trade practices which was enacted by Congress in 1916. If it were modified to effectively apply to small business, it would at least allow a small company to recover compensation from the party causing the injury. A private right of action provision is in H.R. 3 which is being considered by the Ways and Means Committee.

Our third proposal is aimed at diversionary dumping. We believe it reasonable for administrating authorities to be alert for the possibility of this kind of dumping by monitoring the increases in imports or downstream products that are likely to be vehicles for diversion.

U.S. producers would identify products in which the dumped or subsidized output is likely to be used as a major part, component, or material. The Commerce Department would refer lists of these downstream products to the International Trade Commission for monitoring.

If this system were in place, it might detect what we believe is diversionary dumping. For example, we are presently seeing 15 to 20 percent reductions in pricing on foreign sourced gear products, despite the major shift in exchange rates. Ultimately, the Commerce Department would investigate if there were dumping and private industry would initiate a trade case if appropriate.

Fourth, as I mentioned, Federal trade procurement is currently exempted from commercial trade law, allowing known violations to continue. If this Congress were to lift that exemption, allowing trade remedy cases to be filed where bona fide evidence exists that a foreign source product was purchased at below market prices, small manufacturing business would be able to address this situation.

Last, Section 232 of the Trade Extension Act of 1962 allows for cases to be brought and relief to be granted due to imports that threaten U.S. national security. It is essential that petitions in these cases be given the certainty of timely Government responses. At present, however, there are no strict time limits on presidential decision-making in this case.

For example, a Section 232 petition filed by the National Machine Tool Builders Association in March 1983, it took more than 3 years to get a presidential decision. We, therefore, support H.R. 3's shortening of Section 232 timeline for decisions by the Secretary of Commerce.

Thank you for this opportunity to visit with you today. The small manufacturing businesses continue to be bankrupted by unfair foreign competition, while large corporations that are often our customers go offshore. In the interest of maintaining a strong U.S. industrial base and defense industrial base, we urge you to develop a strong and aggressive small business trade title.

Thank you, Mr. Chairman.

[Mr. Bailey's prepared statement, with attachment, may be found in the appendix.]

Mr. MAZZOLI [presiding]. Thank you very much, Mr. Bailey, and I apologize for the slight confusion for a moment as we switched chairs here.

What I think the chairman wanted was to hear from all the witnesses and then perhaps open for questions for those of you who can remain. Ms. Susan Garber, State Director of the Small Business Development Center of the State of Pennsylvania. You are welcome and we are glad to have your testimony.

TESTIMONY OF SUSAN M. GARBER, STATE DIRECTOR, PENNSYLVANIA SMALL BUSINESS DEVELOPMENT CENTER

Ms. GARBER. Thank you, Mr. Chairman.

I manage the SBDC Program for the State of Pennsylvania, which, very briefly, is a university-based 13-center operation with over 60 county offices serving the State of Pennsylvania. Primarily, we provide consulting and training assistance to small companies in a whole range of business subjects.

Just to give you an idea of the scope of the program, since 1980, we have worked with over 69,000 small businesses in the State of Pennsylvania. Just in 1986, we had over 9,000 people who attended training seminars, and more than 6,000 people with whom we provided individual consulting.

At this hearing——

Mr. MAZZOLI. Just a second. You say 69,000 small businesses in 6 years?

Ms. GARBER. Yes; 6 or 7 years.

Mr. MAZZOLI. Those are separate businesses—not repeated contacts from the same businesses? That is amazing. OK.

Ms. GARBER. It is a big State.

Mr. MAZZOLI. You are busy, busy people.

Ms. GARBER. It is a big State, and we have a lot of people.

I have been asked in this hearing to focus primarily on some of the competitive problems which have confronted Pennsylvania's businesses in a newly competitive economic environment, and I will then talk a bit about some of the initiatives we have undertaken in Pennsylvania to help increase the success potential of our smaller and mid-sized companies.

Just to give you a little background, Pennsylvania, like many other Northeastern States, in the last 30 years, has undergone a transition from an economy which was built on farming, mining, and factories to an economy now confronted by different economic forces which demand high productivity, low production costs, high capital intensity, and low labor use. Many of our single industry communities have lost their principal employment companies and much of our manufacturing base in central Pennsylvania has been diminished.

Clearly, service sector firms have replaced some of this revenue base, but it would be naive for us to believe that we could develop a solely service sector economy.

One of the primary initiatives that has been undertaken in the last 2½ years in Pennsylvania is the establishment of the Ben Franklin Partnership Program. Clearly, in response to the susceptibility of our businesses to the vicissitudes of our traditional industries, we have encouraged the diversification of the State's economy by creating four advanced technology centers in four locations throughout the State.

Each of these centers has chosen to select three or four areas of research in which to concentrate its development efforts, and in addition to capitalizing on the strengths of the affiliated institutions, we have tried to capitalize on the strengths of the regions which are served by each advanced technology center.

We do research in areas from CAB/CAM, to polymers, to technology to benefit the handicapped, to specific work in the coal-technology industry. The research and development effort or emphasis of the Ben Franklin Partnership has been vitally important, but equally as important and recognized by the program has been the need for providing support services to the entrepreneurs. This assistance directly creates jobs and helps retain jobs.

The Small Business Development Center network has basically been the key to the delivery of these assistance services in the State of Pennsylvania. In the past 2 years, the technology-based companies that have been counseled by the SBDC have created 653 new jobs in the State and retained another 864 jobs.

The unique aspect of the SBDC Program has been its ability to demonstrate that true partnerships can be developed with Federal and State governments, universities, and the private sector. Although the SBDC's mission is fairly broad and designed to serve all businesses, nearly three-quarters of a million State dollars and approximately an equal amount of Federal dollars have been directed specifically at companies which we call advanced technology companies.

Our efforts at the SBDC have focused in two ways. One is the formation and growth of technology-based companies, and the other is the ability of existing companies to incorporate technological innovation into their more traditional operations.

The problem, as addressed earlier by Mr. Hale, is that the companies do not have the necessary technical knowledge. There is an educational gap. For some of the firms in Pennsylvania, they will be able to provide their own in-house expertise or purchase from the private sector the technical knowledge necessary to make innovations.

However, for a much larger number of businesses, acquiring the knowledge of technological solutions or applications for their products is haphazard. Small companies cannot employ a large or diverse enough staff to incorporate and implement technological changes. Many companies are not even aware that new technologies exist which could serve them well, help them increase productivity and reduce costs.

It is also well-documented that a lack of management expertise is the leading cause of business failure, and this permeates the entire business sector.

What I am saying here, basically, is that we have several problems of small innovative companies: Their resources to implement technologies are scarce; their awareness of technologies is limited; and generally their management skills, business management skills are weak.

In order to help solve these problems, we have incorporated into our basic assistance a number of specialized activities. At our Lehigh University Small Business Center, we are proposing the startup of a technology audit process which would enable us to go into small companies and determine where technology can help them. This has been done in other parts of the State with excellent results.

Our Office of Small Business Legal Services at the Wharton SBDC has done a tremendous amount of work in the area of intellectual property protection and in initial corporations.

Primarily, though, we do business planning and financial planning and that is the bulk of what our companies need. As an example, we have had a number of businesses that have come to us with sort of a typical story, where an inventor has come up with a way to improve a manufacturing process. It has been tested. It has been proven to be a better mousetrap, so to speak, and basically they cannot get to the next step. Usually the inventors do not have the time or do not have the techniques and the talent to bring the product to market. So, this is left to somebody else, and usually those companies end up coming to us.

They are normally advised to contact one of their small business development centers locally and we will work with them on putting together a financing plan. An example that I have used in my testimony was a client at St. Francis College in the middle of the State, a small company, called Denver X-ray in Altoona. They had developed a stress measurement process using a fiber optic system that was a major improvement over former processes.

They came to the SBDC June 16, 1986. They worked with the SBDC on creating a financial proposal which used both private investor, commercial, and Government financing. In July, which was a month later, the company received approval for a commercial loan request of $75,000. They received another $75,000 from the Altoona Economic Development Loan Fund, and they will also soon be receiving $150,000 from a private investor group. This company is now a tenant of the Altoona area incubator and will soon be hiring and training employees. The company sees a bright future.

Another example is a company in the Harrisburg area of Pennsylvania, where an engineer, who worked for a larger company, developed a product to use a computer to improve the fuel-air mixture of furnaces. He was seeking financing, came to the SBDC, and again, we put together a financing plan. He found a bank that was willing to provide loans for equipment and working capital, and he received a $100,000 grant from the State's Ben Franklin Partnership. The firm has grown and the SBDC has continued to do financial planning with them to get additional funding. They are also housed in an incubator in the Harrisburg area. They now have eight employees. They are beginning to make a profit. They have developed a national distribution network and have begun to export the computers to both Canada and Central America.

These are all startup situations. In addition to that, we work with existing companies on technological problems. Bucknell University in Lewisburg, PA, has worked with many companies as diverse as a candlemaker to a company producing circuit boards for IBM. This company came to the SBDC with more of a technological problem than a business problem.

It was using a solvent that they were concerned was toxic. They were pouring it down the sewer. Clearly, the new hazardous waste regulations were beginning to prey on them a little bit, and they decided to come find out what problems they might really have. They had an electrical and an industrial engineer on their staff, but had nobody with a chemical engineering background.

It was determined after analysis that this was a toxic solvent and after a fair amount of investigation, it was presented to them that the only alternative to dispose of this product was terribly expensive, and it was turning out that for the 75 drums a year of this solvent that they bought, the cost of disposal was equal to the cost of buying the product in the first place.

The SBDC identified a chemist at the university who developed a still to recycle the process. By use of the still, they ended up keeping the solvent and they now need to purchase only five drums of it a year and they have no cost of disposal and obviously no toxic waste.

These are individual counseling cases. In addition to that, we do a tremendous number of seminar and educational programs, which continue to be a way to bring to companies new production processes, innovative technologies, and related subjects.

Some of the seminars we run are very technical, such as computer-assisted measurement and control and microcomputer accounting. We have run a fair number of seminars on the hazardous waste regulations. We recently had over 200 people attend such a seminar in Pittsburgh. We ran a seminar at Wharton on building a successful applications software company and over 300 people came. I did not think there were 300 people in the world who did this, no less, in a very small radius.

I think a role which the SBDC's have successfully played in the communities is what we call the role of the honest broker. By being university-based, nonpolitically affiliated, we have been able to put together some unique partnerships with many diverse participants. One of the things we recently did which was very well received was a joint venture strategies seminar, which is another way to improve the competitiveness of small companies.

Many of these companies are stymied with entering the marketplace with a new product. Often, the companies require the marketing muscle, sophistication, and credibility of a larger firm to provide the mechanism for entry. We have worked with developing these strategic partnerships between small and large firms, and a seminar in which we did bring together small companies with large firms ran all afternoon and based on attendee demand, people just stayed until after 8 o'clock at night.

The university's role in this—and the SBDC's role in this is basically to provide an access vehicle, a way to transfer information which will help solve the perpetual problem that small business owners face, and that is the problem of capacity. These business people—and to use an analogy which I have used before—are constantly trying to hold the water back. You can envision these people standing with their fingers in the dike and the water is coming up and they just do not have time to breathe no less figure out a way to get out of the problem, and each day-to-day problem that comes up is like another hurdle.

It is our role to help them over these hurdles. If we believe the data that says small companies are 25 times as effective per research and development dollar as large companies, then we have to assume that there is a role to play here. We must use that innovation and capitalize on it, continue to develop linkages and create opportunities for companies to work together with more large corporations, with Government organizations, with universities, and with other representatives of the private sector.

We must take advantage of money or enable small businesses to take advantage of money that has already been spent by these companies and Governments and universities to establish beachheads in the areas they are trying to enter.

It is the SBDC's role to make that happen, to create new ways for small companies to work efficiently and effectively and to use the natural advantages we have.

I want to thank you for this opportunity to testify and I would be happy to answer questions.

[Ms. Garber's prepared statement may be found in the appendix.]

Mr. MAZZOLI. Thank you, Ms. Garber.

May I say the next time you are looking, maybe you might call Congressman Sisisky or me. Our States are Virginia and Kentucky. We know a little something about stills. Everything else, but that for sure.

Mr. Ciccarelli, the State Director of the Small Business Development Center, State of Massachusetts. How did they let a guy named Ciccarelli in? I thought everybody had Irish names up in Massachusetts. I guess they have Italians up there, too.

Mr. CICCARELLI. No; pretty solid Italian group that tries to keep the Irish out.

Mr. Mazzoli. Keep the Irish——

Mr. Ciccarelli. Keep them honest.

Mr. Mazzoli. OK.

TESTIMONY OF JOHN F. CICCARELLI, STATE DIRECTOR, MASSACHUSETTS SMALL BUSINESS DEVELOPMENT CENTER

Mr. Ciccarelli. Thank you, Mr. Chairman, for the opportunity to testify today, and I commend this committee and the leadership of Chairman LaFalce to incorporate a small business title in the trade bill to be considered by the Full House.

I am John Ciccarelli, State Director of the Massachusetts SBDC, which is located at the University of Massachusetts, Amherst School of Management. Our program is now in our seventh year. During that time, we have counseled over 12,000 small business owners and have provided training to an additional 19,000 small business owners.

We have been successful in helping to generate about $75 million worth of financing for our small clients, which has resulted in about 3,600 new jobs created.

Mr. Chairman, over the past several weeks, this committee, during its hearings on the fiscal year 1988 budget, and now its hearing on international trade, has heard testimony both pro and con on the SBDC Program, and I would like to begin my testimony by dispelling some of the erroneous notions about the SBDC Program.

First, that academic involvement is inappropriate to serve small business. If one looks at the Massachusetts economy and what has happened to the Massachusetts economy, we realize that a very important partner in that development has been the academic infrastructure that resides in our State.

The Route 128 belt and now the Route 495 belt owes a great deal to the innovation and the technology that came out of our academic infrastructure. Our State sees that as an incredibly important component to maintain if we are going to move into the future, and under Governor Dukakis, who has created the Centers of Excellence Program, which is now more formally linking education, the private sector, and Government to deal with specific-defined technology areas, such as microelectronics, polymers, photovoltaics, marine biology, and biotechnology.

Again, it is the creation of this partnership and letting each partner provide their role which enhances the total picture, and likewise the SBDC's being located in institutions and in educational institutions, we are creating and bringing to the table a new partner.

Congress, in its wisdom, when it created the SBDC Program, created it on the basis of a partnership, a partnership not only in name but in financial support. In our State, we receive financial support from not only SBA but the executive office of Economic Affairs, which provides our entire cash match. Then each individual consortium member in our system provides additional match in the form of a contribution of indirect costs back into the program. So, the maximum amount of dollars are being placed to serve small business.

This partnership, though, has to be constructed very carefully. There is a very delicate balance that we all must develop because, as you develop that balance, it enhances each entity's ability to provide the needed services to the small business, and what happens then is the possibilities become absolutely endless in what can be done for small business in the form of management assistance, technological assistance, helping in terms of finance and developing finance market analysis, international trade, and numerous other areas.

One of the comments that we hear continually is that our counseling is done by graduate students and faculty. Unfortunately, that could not be further from the truth. In our program, all of our counselors are full time, all of them have had significant business backgrounds, and throughout the country, many of the counselors who are providing assistance to small businesses are full or part time with significant business backgrounds.

What happens is they are supported by faculty members who come in on very specific projects. They are supported by MBA students in a very controlled environment to do very specific types of projects, such as market analysis. We have at the University of Massachusetts over 60 market data bases, both national and international. We can get an MBA student, a marketing major, to get over to the library, pull all of that information, look through the reference material, bring it back to our counselor, and then jointly they analyze it to help that client in identifying the market nitch that they are looking for.

I have included in my testimony a chart which we did in 1985 and with the Chair's permission, we are updating right now and would like to submit that updated chart to the committee.

Mr. MAZZOLI. Without objection, when it is ready, you can send it in.

[The chart referred to follows Mr. Ciccarelli's prepared statement and attachments.]

Mr. CICCARELLI. Thank you.

Very briefly, as you can see, all of our SBDC State directors have had private sector experience. For instance, the Maine SBDC director was formerly an investment banker on Wall Street. The South Carolina SBDC director had been in the banking industry for over 20 years before he came to the SBDC. I myself have worked my entire working career in economic development, first with the State Office of Minority Business Assistance in Massachusetts, then as the first deputy commissioner for Small Business Assistance, and now as State director of the Massachusetts SBDC.

In addition, Mr. Chairman, you will see that we work very closely with the private sector. Anywhere from 70 percent of an SBDC's counseling load and 90 percent of its training is delivered by the private sector in a partnership effort.

In Massachusetts, for instance, 64 percent of our training was done by private sector individuals. What that relates to in real numbers is 192 of our 292 trainers at our various programs were private sector individuals. They see our program as a very appropriate way of leveraging their resources to help small businesses who, at this point, cannot afford their services but hopefully will be coming back to them as they begin to grow and prosper.

Very quickly, let me indicate a couple of things that show the importance of this partnership. First, as the chairman mentioned, we are in the very preliminary stages of bringing a sophisticated new statistical process control service out to smaller manufacturers in our State.

The University of Massachusetts was contracted by a major auto manufacturer to develop a system for them, not only the software, but also to train the on-line people of how to fully implement a statistical process control program.

We have now begun discussions with those individuals who are developing this process to look at how we can simplify it for smaller manufacturers and then take it out to them in a joint effort of both training and then direct counseling.

What we are hearing in Massachusetts from many of the major corporations is that quality control is critical in dealing with their smaller manufacturers. Many of them are asking their smaller manufacturers and their smaller vendors to institute a statistical process control system.

We are hopeful, with the technology developed through a contract with a major auto manufacturer that we are now going to be able to refine it and bring it to the small business community and the small manufacturers. We are very excited about that.

I think there is no better avenue to link the technology transfer issue, international trade, the management assistance component, which is so critical to small business, than the SBDC Program. There are 49 SBDC's now in the country, serving out of over 600 cities and towns. It is a network that has incredible potential, and as the partnerships continue to grow with State government, with the Federal Government, with the academic institutions, and particularly our technology, our engineering programs, we are going to be able to do more exciting things for small business, but what we must keep in mind and what is very important is the fact that within our engineering programs to bring this technology out to small business, we are dealing, when we go to that table, with larger corporations who have significant financial resources, to provide to our engineering programs, and we need to be on that same level with them if we are going to bring this technology out to small business.

We have to facilitate it. We have to be the honest broker in that situation, but we need the resources to do that.

The SBDC Program in terms of not only the technology transfer but the management assistance end is critical. In our State, we have over a dozen quasi-public financing programs. We are now asked to participate with them at their monthly meetings because management assistance is key to developing the kinds of packages necessary to help these businesses get funding. We need to help our small technology base firms who many times do not understand the financial mechanisms and the financial process that they have to go through. We also need to be working with our more mature industries, our smaller manufacturers, who are looking for new processes, to bring new technologies in, to help them in doing the market analysis necessary to get into new areas as well as help them to then utilize the financial capabilities that exist not only in our State but from the Federal Government and our conventional sources.

This is an important aspect of our program. We have established a Capital Formation Service and in its 4-year history, two individuals have helped small firms in our State obtain over $31 million in financing. Five regional centers have added to that, helping to obtain $44 million, which brings us to our total of $75.

Again, the importance of working with all components of a business, of bringing that holistic approach—not just technology transfer or international trade—the holistic approach to servicing small business is key, and I think the SBDC Program is in an excellent position to do that as long as the partnerships are developed and can be developed with the Federal Government, the academic institutions, and the private sector and State government and local government.

It is an exciting program. There is much that can be done and we thank you very much, Mr. Chairman, for allowing us to testify and to obtain your support.

[Mr. Ciccarelli's prepared statement, with attachments, may be found in the appendix.]

Mr. MAZZOLI. Thank you very much, sir. We appreciate that testimony very much.

Now we will have Mr. Gregory Higgins, who is the State Coordinator of the Small Business Development Center in Pensacola.

Mr. Higgins, welcome.

TESTIMONY OF GREGORY L. HIGGINS, JR., STATE COORDINATOR, FLORIDA SMALL BUSINESS DEVELOPMENT CENTER, PENSACOLA, FL

Mr. HIGGINS. Thank you, Mr. Chairman.

For me, it is a real pleasure to appear before the House Small Business Committee because it gives me the opportunity to personally thank the committee for the support and encouragement they have provided to the Small Business Development Center Program over the years.

In the context of your deliberations on ways to increase the international competitiveness of small- and mid-sized U.S. companies, I have been asked to provide a brief overview of a pilot program in international trade development which Florida has just begun. Since this pilot program only started in January, I can promise you it will be a brief overview.

Mr. MAZZOLI. That is all right. Succinct.

Mr. HIGGINS. Before I describe the goals and the scope of work of the program, I would like to take just a moment to give you a little background on the setting of these international trade development efforts.

Florida has a substantial Small Business Development Center Program. In a period of a year, we will run over 700 seminars in the State with about 26,000 people in attendance. We will counsel, that is, provide one-on-one counseling for another 12,000 clients.

Now, we, until January, did not have a formal program, but even within our existing program, we did put on about 10 export development seminars attended by about 300 business persons and in that same year, we provided one-on-one consulting—about 600 hours of consulting—to another 132 clients involved in export.

We also have, in the past, made an effort to train our consultants so they will have a general knowledge of the management problems faced by exporters and if they cannot provide the assistance directly, they can make intelligent referrals on matters of international trade development.

Until this January, we had no formal, structured, international trade development program; and our level of involvement was dependent upon demands of clients and the expertise of certain individuals with our system.

Even without a structured program we did identify several important characteristics of international economic activity of small businesses in Florida. First, it was very obvious to us that there was a high level of interest in and also a high level of uncertainty about becoming involved in international trade.

It was also apparent to us the programs, such as those operated by the Florida Department of Commerce and the U.S. Department of Commerce, while they were very successful in some aspects of trade development, did not have the resources to provide the one-on-one management assistance that is frequently required of a small firm as they attempt to enter the international market.

Finally, we recognized one of the problems in our State was the shortage of individuals with expertise in international trade. Specifically, we found that within our State university system, and we are a university-based SBDC, while some courses in international trade are offered, these courses tend to be heavily theoretical and are not really, for the most part, designed to prepare students to participate in international trade.

So, it was against that background that we decided we would go ahead and develop a pilot program in international trade. What we generally do in Florida before we jump in to a program, is to ask one or more of our universities to develop and test a pilot program to determine if it is cost effective. We will run it for a year or two to see how the thing works before we begin to encourage the other centers to adopt a program. The results of the pilot are then shared with the other centers to modify and adapt to meet the needs of their particular service area.

In the case of the International Trade Program, we requested proposals from our participating universities and selected the one designed by Florida Atlantic University, which is in the Boca Raton-Fort Lauderdale area, and Florida International University, which is in the Miami area.

The area in which we are going to test the pilot is Southeast Florida. We think it is particularly appropriate area because it has a total population of about 4 million, about 130,000 small businesses, a very large Hispanic population, a large number of foreign visitors coming in and out of the area, four deep water ports, and three international airports. In short, if we cannot make it go in this area, we probably cannot make it work anywhere.

Based on that background, let me give you an idea of the scope of work. Now, the scope of work for this pilot has two basic components. One is the service delivery component, and the second is a program development component. Let me describe the first one, service delivery.

Now, while this is a pilot program, we have found that it is more cost effective to go ahead and deliver services you know you can provide and for which there is a demand while at the same time we develop additional capabilities. This is really in keeping with our primary mission which is to make sure that the small businesses receive the management assistance they need.

So, under the service delivery component, we are going to develop and conduct seminars and workshops on opportunities and procedures involved in exporting, importing, joint ventures, and licensing. We anticipate that during the calendar year, we will hold 32 training programs that will be attended by about 900 individuals.

I should mention a point that Mr. Ciccarelli also mentioned. In these training programs, as in all of our training programs, we rely very heavily on individuals from the private sector to make the presentations to the small businesses. The fact is, about 75 percent of the presenters at our training programs are people from the private sector. Last year, I think we had about 440 private sector individuals participate in our training programs.

We have also found that in any specialized program, if it is going to be successful, must have the capability to follow up the training with one-on-one assistance. This is really necessary so that the businessperson can take the information, the general information they learn in the seminar, and in a face-to-face meeting with a business analyst, determine just exactly how that information impacts his specific business.

So, the second component of our program is the in-depth counseling to help the client evaluate his export capabilities, identify potential markets, establish the necessary relationships with appropriate public and private organizations, assess his international trade financial needs and, if necessary, develop an export financing plan, his loan packager to finance his entry into the export market. We will deal with any other specialized business needs that the client may have.

We expect in the calendar year to provide about 2,800 hours of one-on-one consulting to about 230 clients. Now, to help us do this, we have not only our own staff, but we rely very heavily on some expert part-time and volunteer assistance, and, again, to re-emphasize a point that has been made, I want to spend a couple of seconds and tell you about the people that are involved in this because there is a persisting myth that the small business development centers are ivory tower operations that are providing classroom solutions to real world problems and the fit is not all that good. So, let me give you the background on some of these folks who are working with us.

Abraham Garfinkle, he is a retired garment manufacturer and international marketing expert, who has completed 7 overseas projects for the United Nations Industrial Development Organization, and has been a counselor for the International Executive Service Corp. in 10 overseas projects in South and Central America, Asia and the Philippines.

Andreas Papademetriou is a seasoned importer-exporter with a long career in international trade that took him to five countries on three continents over a period of 35 years. He is a member of the American Management Association and of the board of directors of the Fort Lauderdale/Broward World Trade Council.

Al Redlhammer is a former director of the Port Everglades Foreign Trade Zone. He is currently president of Sea Riders, international freight forwarders; and president of Sea Riders Brokerage Corp., a customs brokerage involved with land, air, and ocean shipping all over the world. His international business experience spans 24 years.

John L. Strudwick, a graduate of the International Marketing Institute of Export in London. He is currently Florida International University Small Business Development Center Program coordinator, instructor, and consultant in international business, member and former director of the World Trade Council. He has 30 years of marketing experience in a variety of foreign markets.

Mel Zilinsky is a member of the National Association of American Export Companies and has worked for 30 years in wholesale importing-exporting in Europe, Asia and South America.

So, we think with these folks and with our own staff and with our access to the faculty and the graduate students of the universities we might be able to actually provide some realistic assistance to small businesses.

The second major component of this pilot effort, is program development, and generally this scope of work includes the generation of checklists for evaluating clients' potential business capability for exporting or identification of existing lists which might be useful. I have a feeling there are thousands of lists out there. It is a matter of identifying ones that are particularly appropriate for the kinds of small businesses we deal with.

Development of lists of international trade organizations through which the center will conduct its coordinated program. As I said earlier, there are a lot of organizations involved, and we certainly do not have sufficient resources to waste by duplicating capabilities that exist elsewhere.

The third item is the development of general public relations material, preparation of outlines, and presentation aids for the seminars. As I indicated earlier, we have identified a need to increase the ability of the State university system to produce individuals ready to enter the international market. To meet that need, we added some additional items to the scope of work.

The university will be required to design a program to use graduate and undergraduate students in the delivery of services to clients. They will be required to design a graduate internship in international trade development for small businesses. This internship would allow the student to earn graduate credit while working with the Small Business Development Centers in international trade development. Parenthetically, that will give us a free resource for a period of time.

The university will be required to develop another type of graduate internship in international trade with graduate students working in the private sector. Because this is a pilot program, we will require that a manual describing the center's organizational structure, functions, and operational techniques be developed so it can be shared with the other centers in Florida and any other institution that is interested.

Also, the center will be required to design and implement a procedure for measuring the effectiveness of the program. The procedure must assess the views of the clients and other organizations participating in the program. The analysis and explanations of successes and failures will be available to all the centers. That is basically what we propose to do in the pilot, and as I said, we started in January, so we do not really have a great deal to talk about in terms of results, but the program is moving forward.

I have provided some material on two of the educational programs now underway. One is entitled the "Program for Exporters of American Products and Services." That is a four-part training program combining classroom instruction with hands-on experience and one-on-one counseling. The other is a program entitled "Exporting High Tech," and this will feature a number of speakers addressing how to research markets, marketing techniques, export restrictions. It will also include panel discussions on specific industry needs.

We also, I think, have been able to generate some international interest. We are working with the Guatemalan Government now to move an entire trade fair to the campus of Florida Atlantic University and are working with some citrus growers in Indian River County on possible exports to Japan. We have reached an agreement with the Government of Jamaica to cosponsor a series of seminars on trade with that country. We have planned a day-long conference entitled "Focus: The Middle East," to take a look at potential markets in that area.

The primary problem we have encountered so far has been the demand for this kind of assistance. As the program gained visibility through press releases and through our own mail-outs, the demand threatened to swamp the staff. For example, in the first educational program I described, there were twice as many people interested as we were able to accomodate.

I have advised the center to cut back on the publicity until they spend a little more time generating the capability to handle it. I am confident we are going to have a successful program and we certainly appreciate the interest and support of the committee.

Thank you.

[Mr. Higgins' attachments to testimony may be found in the appendix.]

Mr. MAZZOLI. Thank you very much, Mr. Higgins.

Our last witness today is Mary A. Wathen, president of Koboway, Inc., Costa Mesa, CA, who is representing the American Electronics Association.

Ms. Wathen.

TESTIMONY OF MARY A. WATHEN, PRESIDENT, KOBOWAY, INC., COSTA MESA, CA, AND REPRESENTING THE AMERICAN ELECTRONICS ASSOCIATION

Ms. WATHEN. Thank you, Mr. Chairman.

I am President of Koboway, Inc., as you just said, in Costa Mesa. We probably have a little bit of a different perspective than some of the other witnesses, I think, that appeared here today.

We are a small business. I employ about a 145 people. We are about a $12 million corporation. We have been in business since 1972. We have come through the gamut of lots of things.

In the last couple of years, though, the number of independent circuit board manufacturers have decreased dramatically in the United States. We used to be about a thousand. We are down to about 600 now. The reason for this is because many of the companies are now moving their requirements offshore. They are buying from offshore types of organizations rather than buying locally or buying American as such.

There is a variety of reasons why these firms choose to go offshore, and many are directly related to the tax, trade, and regulatory environment here in the United States. I will discuss some of these.

I am also here today representing the American Electronics Association, which is the Nation's largest high-technology trade association, consisting of 3,250 companies across America. Most of our membership is in all different segments of the industry and three-fourths of us employ fewer than 250 people.

The network of these people ranges across the United States and there is about 2½ million people employed in electronics here today.

The work of the House Small Business Committee is of great interest to our membership. I think, as the chairman spoke originally, he said that the Federal Government can play a catalytic role in what happens with small businesses, and we certainly heartily agree with that. We think on trade policy that we have to come up with a way of increasing exports rather than limiting imports into the United States. We have to be allowed to export our products, and simplify the process to make this happen, but we have to be allowed to do that.

On the issues of tax policy, raising the tax rates would hurt small businesses, but technical corrections will help them. As far as procurement is concerned, regulatory impediments limit the ability of small businesses to contribute to a small national defense. Occupational safety is another important area, and it is necessary in the work place, but without new administrative burdens.

Electronics is a very vital segment of the American economy, and a toolmaker that enables other industries to strengthen productivity and competitiveness. Between 1978 and 1984, the electronics industry created over a million new jobs in the United States. We now employ, as I said, 2½ million Americans, and many more are indirectly in other related industries.

When I was flying here yesterday from California, I thought it was quite interesting. There was a news cast that came on as they do on the airlines, as you are flying, and this newscaster said, when we think of electronics, you think of Japan. I find this a very disheartening statement to say the least. I am certain he was talking about consumer electronics, not industrial electronics, but the mere fact that that is peoples' idea of exactly what is happening in this industry, I think, is unbelievable that we are allowing this to happen, but I think that is probably a true statement.

One of the very major, important things, I think, is our trade policy, as I said, to increase exports rather than limiting imports. We do not look to Congress to legislate the trade deficit away, but we believe that it is the responsibility of industry to compete more effectively. How the U.S. Government shapes economic environment in which we do business. In particular, we in industry must rely on the U.S. Government to eliminate overseas barriers which restrict our access to foreign markets as well as unfair advantages which our competitors receive from their own governments.

Within the last month, I believe, I have had three independent inquiries from companies in Japan that were looking to buy our technology here in the United States. These three different companies wanted to buy a percentage of my company, 10 percent of it, so that they, indeed, could buy the technology that we currently have and they wanted that technology here in the United States, not in Japan. I find this quite an interesting development to say the least.

The AEA believes that trade law reform should be designed to increase the access of U.S. companies to overseas markets. To help achieve this objective, AEA supports launching a new round of multilateral trade negotiations as well as the aggressive enforcement by the Government of U.S. rights against foreign unfair trading practices.

In addition to these measures, unnecessary disincentives to exports must be removed. In particular, national security export controls, which are required to prevent the Soviet bloc from acquiring U.S. technologies, are administered in a way that places U.S. firms at a disadvantage in competing in western markets.

I was also reading in the Electronic News, coming over here, that one of our major companies in the United States, which is Cray Research, was recently not allowed to export a $20 million system to India for these kinds of reasons, because it was a four-tier computer. They would allow them to export a two-tier but not a four-tier. NEC, again, a company in Japan, will now go in there, of course, and sell this $20 million system to India, and, again, we are not being allowed to compete on this level ground.

Another very important issue, of course, is raising the tax rates, and the reasons that business groups supported the 1986 Tax Reform Act was its provisions to reduce the basic corporate rate from 46 to 34 percent on July 1, 1987.

However, we are quite concerned or quite worried that they are going to want to freeze these tax rates at today's rates rather than, indeed, allowing these rates to go down. Electronics companies, in general, historically, pay a very high tax rate. My company, even though I am very small, I am still paying on about the 45 percent range as far as tax rates are concerned. I really do believe that we all should pay our fair share and think that it is important to do so, but we would like to see that which we strove so hard to do—reducing that tax rate to 34 percent—really allowed to go through.

We talked about research and development, the R&D tax credit that is now going to expire. We feel it is a very important issue, if we are going to be allowed to compete, again, with our global competitors as such.

In the printed circuit board industry, we have various levels of technology. It starts with the basic single-sided circuit board, goes up to a very sophisticated 17- to 20-layer circuit board. To begin with, single-sided boards, double-sided boards, and very simple four-layer boards, all went offshore, and we as manufacturers realize that this was a trend we were not going to be able to stop. We really kept increasing ourselves and growing up into the higher technologies.

If we are going to be able to compete, we have to keep technology here. We have to be allowed to invest in R&D to stay competitive and to be able to produce this higher-end technology. If we stop moving, the 600 companies that are now here, which are independents, will certainly go away as well. We are not unlike the semiconductor industry. We work very much in parallel with them. We make that basic product, but they have nothing to put their semiconductors on if we do not manufacture that basic board. If we allow them to go offshore in its entirety, we will be just bringing back completed assemblies and we really will take a giant segment of manufacturing out of the United States.

If we can keep this R&D tax credit as such, it allows us to be able to compete and it also then is important that it stays in for startup companies, not just in existing technologies, or we are not going to be able to come up with that new widget in a few years from now, instead that the Japanese, of course, are going to want to buy from us as they want to buy from us right now.

A top priority for the AEA in 1987 is to implement the statutory preference for nondevelopmental items, commercial products enacted in 1986 as a section of 907 of the Federal Authorization Act. AEA is a cofounder of COMPACT, Coalition of Industry Associates and Companies interested in selling commercial items to DOD to replace identical or similar manufactured items according to detailed military specifications.

We find small businesses, though, are at a disadvantage in dealing with the Government as prime contractors certainly because of the intense auditing and negotiations that have to go into contracts. A lot of us do not have on staff the kind of expertise that you need to be able to really negotiate a deal to come back along and to make your cost accounting practices, and so forth, stand up to the rigors of all the audits that happen, even not necessarily as a prime but as a subprime. My company is about 41 percent in the military and aerospace right now, and we deal with all the large prime contractors, and we are fortunate in the fact that we do have the sophistication that we can deal with them, but there are very many smaller companies than ours that really could not sit down in an 8-hour negotiation and be able to hold their own and to defend their practices as such.

I am trying to be brief, so, I am going through these pages here for you quickly. In summary, though, I think there are several competitive obstacles that now face small high-technology companies. I have mentioned the key issues in my testimony that face AEA members, although other committees in the House have primary jurisdiction over some of these issues.

I hope that committee members will add their voices in the House for the electronics industry and advocate changes that will help improve the economic environment in which we compete, and I do thank you for this opportunity.

[Ms. Wathen's prepared statement, with attachment, may be found in the appendix.]

Mr. MAZZOLI. Ms. Wathen, thank you very much.

All the testimony was excellent. I am sure that it will help Chairman LaFalce and the members of the committee to try to put together a small business title for the trade bill, which is the essence of these meetings. However, you all were invited to go beyond just that narrow topic.

I came in toward the end, but I think Mr. Bailey summed up by saying that we ought to get tougher—some words to that general effect—in dealing with foreign trade and so forth. I think you and Ms. Wathen seemed to deal with that subject, and I want to come back to the small business development people with a couple of questions.

But first, may I ask you how you see us getting tough? If we were to get really tough and build these walls, that would hurt the very people that Ms. Wathen stands for. She says that they have to have some opportunity to increase their exports or they are in very grave trouble.

Can we be tough without putting up protectionist walls?

Mr. BAILEY. Absolutely.

Mr. MAZZOLI. OK. Do you want to tell me how we can do it then?

Mr. BAILEY. We think that if we can get on a level playing ground with the rest of the world, we would be quite comfortable.

Mr. MAZZOLI. Let me stop you there because I have heard that. Competitiveness and level playing field. Does a level playing field mean that we have got to force Malaysia or some emerging nation to pay every one of their workers $30 an hour like we pay ours? Is that what it means? What is a level playing field?

Mr. BAILEY. If I were a worker in Japan, I would probably receive something in the neighborhood of a comparison to our automobile worker who might be making $16 an hour, maybe $7 an hour.

Mr. MAZZOLI. Is it not higher than that now?

Mr. BAILEY. What?

Mr. MAZZOLI. Is it not edging up higher right now?

Mr. BAILEY. Yes, yes; but more importantly than that, the Japanese Government through MITI would sponsor research and development into how they could make, for example, their cars cheaper. That research and development is the kind of thing that we do not have. We really do not, and that is where the problems lie. That is merely one small hole in the wall, but it is this sort of thing.

For example, MITI alone using that example is, as you know, almost a national concern that directs everything that happens within the economy. We do not have anything like that.

Mr. MAZZOLI. I understand that we used to do that. But MITI is not picking the winners and losers as much anymore as it used to, and there are an awful lot of losers and they are surprising themselves.

Mr. BAILEY. South Korea, for example, has now developed such an incredibly good steel mill portion of their economy that the Japanese cannot compete with their steel.

Mr. MAZZOLI. That is exactly right.

Mr. BAILEY. So, MITI is saying let us get out of the steel.

Mr. MAZZOLI. Well, I guess what I am trying to suggest or at least to get at, is that one of the problems we have is that the world is such a dynamic place and it is so quickly shrinking. I saw something in the Wall Street Journal the other day that just amazed me. We not only have the problem that Japanese cars are higher priced because of the Yen and dollar valuation, so that they are becoming, sort of, above the fray, but now we have the Hyundai and the South Koreans coming in. But even they will start to feel the heat as Malaysia will soon be exporting cars to the United States, India, Greece. I did not know that these nations had an automobile industry, much less that it was of such a degree of sophistication. Except that the financing is coming in from Japan, the financing is coming in from South Korea. Because if they cannot do it at home, it is like our people. If we cannot do it in the United States, we will do it offshore.

If the Japanese cannot do it in Tokyo or Osaka, they are going to do it in Seoul or they will do it in Qualalempore or something.

The question is can we really, in this kind of a shrinking globe of telecommunications—where they can dismantle a steel mill and erect it in another country—is there some way we can handle that kind of a dynamic role?

Ms. Wathen?

Ms. WATHEN. Well, what I really see and back to one of the issues that I made that one of the most important things to do is that we have to stop restricting the exports, not only what we are trying to do with the imports, but we put such restrictions on our exports that if we are even a small manufacturer with the most terrific idea in the world, by the time we get through the licensing that has to happen and the paperwork that has to happen, then, only have it be shot down. By then we have lost our slot in the marketplace, and Japan or Korea or whomever, can get in there a whole lot quicker than we can get in it.

I recently had an inquiry, again from the Department of Commerce, asking me if I would be interested in manufacturing a printed circuit board to export to Japan because they, indeed, now need to have some imports coming into their country, and I was not because it was a very low technology board, but I would be sure if I would get to the point where I, indeed, would want to build this for Japan, I would never be able to get it exported out of here.

Mr. MAZZOLI. Because of the Export Administration axe?

Ms. WATHEN. Exactly.

Mr. MAZZOLI. Well, a second level computer firm from left field for that matter, but you said a four-level would not make it but a two-level would. Are you afraid at all that we are exporting technology that can come back to haunt us?

Ms. WATHEN. Not really because the majority of that technology is already there, and I think we are very much kidding ourselves that we have an edge on that. What we are really doing is restricting the U.S. manufacturers and not allowing them to compete. It is more that than anything else.

Mr. BAILEY. MITI—just to go back a second. In our area of expertise, we are what you might call a more mature industry and do not really have those research problems that the electronics industry does have.

But we would like to suggest, for example, that in the foreign countries, the government works as a partner in foreign trade and that does not happen around here. We are all familiar with the downstream dumping and all these sort of things that we are trying to get pushed through in this trade bill, and, hopefully, it will be of some benefit to get on the road.

Mr. MAZZOLI. Well, I appreciate that very much.

Just a couple of questions to the people who represent the Small Business Development Centers. Chairman LaFalce is interested, at least as a kind of discussion paper, in perhaps promoting or increasing the presence of small business development centers in this whole question of export, encouraging export.

I think a couple of you mentioned this peripherally, but obviously the majority of your work is done with local businesspeople who are selling domestically, not internationally. Let me ask you to the extent you have had experience with this. The gentleman from Pensacola did talk about your work.

Do you do much of that, Mr. Hale? Any of you? Are any contacts separately brought to you by small business who pick this idea up from reading the trade journals or something else or basically are they still talking about working domestically?

Mr. HALE. No; we find many of our companies in Missouri are interested in international trade. It is something that they think about, they have an interest in, they take the first step or two and discover many of the problems——

Mr. MAZZOLI. It is so immensely complicated.

Mr. HALE [continuing]. And they back away. We have a very, very good department in State government who have the sophisticated capabilities of assisting those companies. We will work with the companies and get them to the point where they have their basic business, their basic management strategies pretty solid, and then we will pass them along to the experts in international trade.

Mr. MAZZOLI. Who are the experts outside of your field? Are they at the university or is there a separate source? Where do you find the experts to deal with?

Mr. HALE. In the state of Missouri we use the Department of Economic Development.

Mr. MAZZOLI. Jefferson, yes.

Mr. HALE. It is a State-sponsored staff in Jefferson City. We also have a very, very active international trade group of the Department of Commerce in St. Louis and Kansas City, who maintain the traditional export links.

Mr. MAZZOLI. So, after you get things organized and squared away, then you move them on to the second phase where they can get into that more intensely.

Mr. Higgins, now, your program is just new and you may not be able to quantify it, but was it in part started because you were getting inquiries from small businesspeople about international trade or did you start a separate format?

Mr. HIGGINS. No; we were getting a great many inquiries. As I indicated, we were dealing with 300 or so clients with just a very few workshops. It was apparent this was an area in which there was a significant interest, but, at the same time there was a lack of understanding about what is involved in entering the international markets.

Mr. MAZZOLI. Has it come about the same way as Mr. Hale is saying—that they start out and get stunned by the complexity of it and back off unless you can take them the next step?

Mr. HIGGINS. Yes, sir; that is basically it.

Mr. MAZZOLI. Ms. Garber.

Ms. GARBER. We have had, I think, a slightly different experience. We have not been active until very recently. We are also in the process of doing a pilot program in Philadelphia out of the Wharton School. We have been doing, for about a year and a half, a very successful program in the Lehigh Valley through Lehigh University, where we have had substantial results and have brought a number of companies into actually exporting.

One of the things we found both in the procurement and the export area is our mission should probably start being more proactive than reactive. When we run conferences, we do get a lot of people. They are often not the companies that are in a position to be in either of those markets, and what we are starting to find out is that we have to go out and find companies in a lot of ways that are well positioned financially and, organizationally, from a human resource capacity, and from a product point of view, and then work with those companies. We have been very successful in the procurement area doing that, where it is no longer enough to have a big conference and have people walk around and talk to purchasing agents and then they come talk to us because most of those companies are not going to be able to do that, and the same thing in the exports.

So, we are really looking to find the companies.

Mr. MAZZOLI. Mr. Ciccarelli.

Mr. CICCARELLI. It has been quiet, I guess, in terms of exporting up to now. What we have tried to do is use the resources that exist in our State. We are fortunate we have an international trade office out of our Department of Commerce, also the Mass Port Authority has had a very successful small business export program for a number of years. So, we have worked hand-in-hand with those people when we have identified clients who could take advantage of those programs, and we have moved them through into that process.

What we are beginning to do right now is, I think, what Susan says, take a proactive role in the whole international trade area. One of the things we are seeing is not only the shock value of my God, look at all this stuff we have to do to go abroad, and we just cannot handle that. One of the ways we are beginning to look at how to address this and it has been done at the university through the Small Business Institute program is provide companies with market analysis. Those who just have a glimmer of the thought of maybe I would like to get into international trade.

The professor has almost totally structured his program into international market analysis. So, the company has then without kind of hitting those first hurdles, they get an identification of what the market potential is. It gives them a greater incentive than to begin the process of trying to reach those hurdles and go over them.

So, we are in the very early stages of looking at it, but at this point, the kinds of clients we have been seeing overall have been very small. About 50 percent of our clients are in the startup mode, so, we are providing services to a group that, at this point, is not that.

Mr. MAZZOLI. Does this have the support of Governor Dukakis? I say that lovingly because I know Mike, and I just want to be sure that his new and more recent advance is well noted on Capitol Hill.

Well, ladies and gentlemen, it has been really interesting, and I want to thank you all for your attention and for the testimony. I am sure that the chairman will pursue some of the points you brought up and the staff will analyze and collate all these suggestions so that perhaps we will be able to put something on paper as soon as next week.

So, we do thank you, and the subcommittee will now stand adjourned.

[Whereupon, at 3:00 p.m., the committee adjourned subject to the call of the Chair.]

APPENDIX

PREPARED STATEMENT OF HON. ANDY IRELAND, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF FLORIDA

Mr. Chairman, I appreciate the opportunity to appear today and testify before the entire committee on the subject of the trade bill and small business. I must first compliment you personally for your vigorous pursuit of the leadership on this issue. As you know I have worked on the trade issue for almost 10 years now, which includes my Eximbank Small Business Amendments which became law several years ago. I am pleased that we now find ourselves at a crucial crossroads on trade.

Again I commend you for securing a separate Small Business Title, and I have mixed emotions about the jurisdictional problem which confines the Title to the activities of the Small Business Administration. At the same time I must say that I believe that our committee has a responsibility to call the needs of the small business community to the attention of the other committees of the House. So if you will allow me I would first discuss the SBA and then offer some suggestions which will loom outside our jurisdiction but which I feel deserve our attention as legislative advocates of the small business sector of the economy.

SBA

The record is clear. At present no one speaks for small business in the upper echelons of federal trade policy. Therefore now may be the time to make the Administrator's slot a Cabinet level position. To do this actually requires only a small increase in pay. It is really no legal nightmare because the Cabinet exists by tradition and not law. I also would doubt any other committee will raise a jurisdictional question. If we were able to accomplish this, we would have one major problem solved - a voice for small business at all crucial upper echelon trade meetings.

Next I would suggest that we replace the current Director Of International Trade's slot with a new agency slot entitled Assistant Administrator for Trade. This individual would then oversee the current office and also would assume any new duties added by the various proposals we are now considering here in committee. In addition, a part of this new individual's duty should be some form of permanent working relationship with the state and local governments and their efforts in the trade area. Anyone who has studied the trade issue knows that the most innovative and constructive efforts in the expansion of exports now occurs in state and local governments. (You might be interested to know for example that at the present time our 50 states now spend more annually on export promotion than does the entire U.S. and Foreign Commercial Service at the Department of Commerce.) We could do worse than to direct SBA's energy and resources to helping these already successful programs.

Mr. Chairman, that concludes my thoughts with regards to the SBA. I would now like to share with you and the other members of the committee some thoughts I have developed in recent years, which I believe would bring about a greater participation by small business in the export markets. I agree with so many who have pointed out that small business is the key to the return of American competitiveness worldwide.

I certainly do not claim that the following list of proposals is complete or that as it stands it does not need some modifications; nor that it does not touch the areas of responsibility of our fellow committees. However, I believe that as a committee, we have a responsibility for what you might call legislative advocacy similar in our domain to the SBA's Chief Counsel for Advocacy's role in the executive branch. I would suggest that we address these initiatives on behalf of small business by perhaps calling our colleagues' attention to their importance in the form of floor amendments or in the record of the floor debate on the final trade bill.

1. There should be appointed a Small Business Assistant Trade Representative within the U.S. Trade Representative's office. At present there are more than 44 Assistants, none of whom deal with small business. It is appalling for this nation not to have a voice at the GATT round, for instance, that can speak for small business.

2. All United States ambassadors should be required to provide a brief annual report to the Secretary of State and the Congress on their export promotion accomplishments relative to small business as well as any innovative programs their host country has developed for their own small businesses.

3. The Department of Commerce should be required to:

a.) conduct a biennial meeting in the form of a national conference featuring small business trade and economic development for the Secretaries of Commerce of the 50 states, the District of Columbia, and the U.S. Territories;

b.) undertake a study of the effects on U.S. international competitiveness of state tax systems, including their effect on small business trade promotion, the utilization of FISCs' and small business capital formation:

c.) instruct the Bureau of Analyses to produce a Gross State Product figure for all states, the District of Columbia, and the U.S. Territories; such figures would further enhance the successful export efforts of the many fine state and local programs.

d.) join in a Small Business Policy and Export Promotion Advisory Commission with the SBA, USDA, and USTR;

e.) increase the term for membership in all Industry Sector Advisory Committees from two to four years; and

f.) do a study to determine the feasibility of merging and/or co-locating the district offices of the U.S. and Foreign Commercial Service with existing state export promotion offices.

4. A study should be done with an eye toward overhaul of the Standard Industrial Classification (SIC) code to determine what industries are overlooked. (As testimony yesterday showed many service industries are not even accounted for which leads one major economist to wonder if we even have a trade deficit.) Also both export trading companies and export management companies should have their own SIC codes, otherwise there is no way we can figure out export statistics.

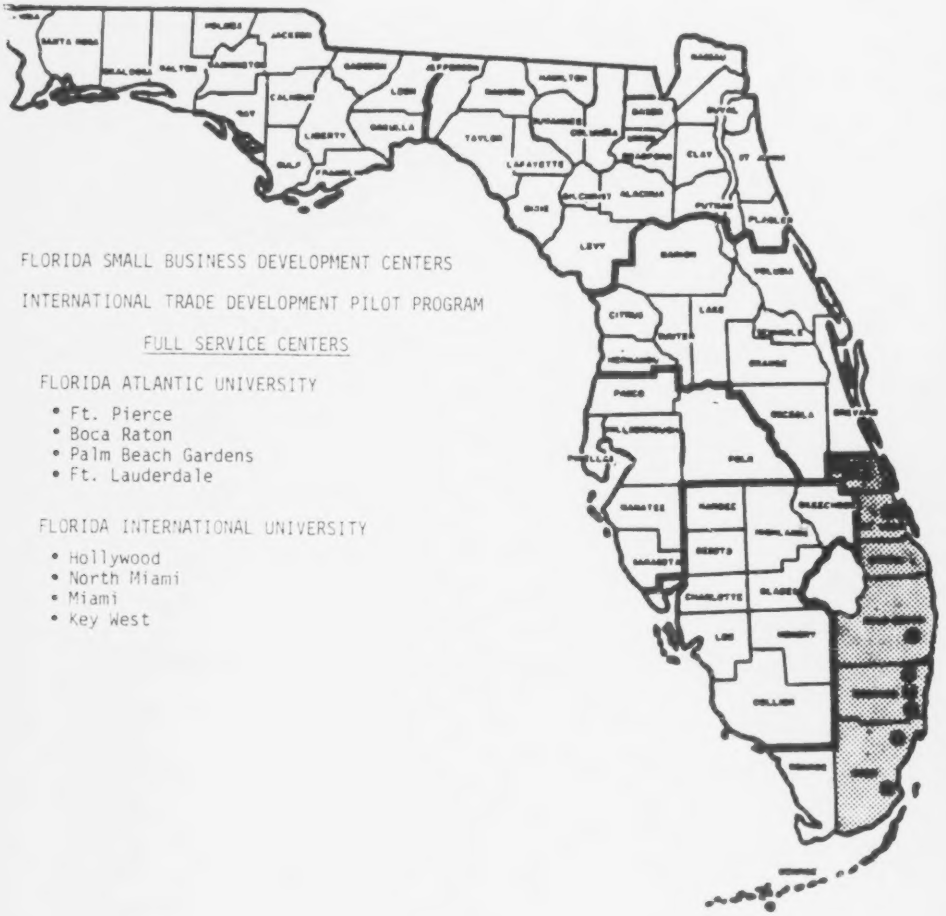
5. The Economic Development Administration should be required to set aside $100,000 a year for each state for the purpose of encouraging state strategic small business economic trade plans.

6. Eximbank and the SBA should consult and report to Congress within six months on a plan to develop risk protection plans for state small business export financing programs with a minimum of 80 percent coverage.

7. The President's Science Advisor should be compelled to have a coordinator of Federal Labs who would serve as a liaison with new small business technology initiatives at the state level.

Mr. Chairman, I thank you for your consideration.

Attachments to Testimony of Gregory L. Higgins, Jr.



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- Ft. Lauderdale

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- North Miami
- Miami
- Key West

TECHNIQUE

The Official Newsletter of FAU's Small Business Development Center

Volume I Winter 1986 Number 3

How Tax Reform will Affect Small Business

After many months of writing, rewriting, thinking, rethinking, amending, negotiating and generally sprucing it up, the Tax Reform Act of 1986 became the law of the land.

But is that good news or bad news? And, as it affects small business, should we worry or rub our hands in glee?

Yes and no. A little of both. It depends on how you run your business and how small your business really is.

The **good news** is that the effective tax rate for corporations is going down beginning in 1987, but the actual tax bills for small businesses may stay the same or even rise. One of the reasons for this is that the top rate on corporate earnings, which is now 46 percent, will drop by 12 percentage points to 34 percent. So if your business is incorporated, and if the taxable income is $75.000 or more, you are likely to see your tax bill drop. On the other hand, if your little corporation has taxable income of around $25,000 or less, the rate will stay at 15 percent.

To make matters worse for the little guy, small business, whether incorporated or not, will be forced to give up many of the same tax advantages as the big corporations. The first of these is the business community's carrot of 1981, the Investment Tax Credit, which could be as much as 10 percent of the cost of capital additions. Not only is the ITC ancient history, but its demise is retroactive to 1986. That means that any equipment purchased in 1986, unless under contract before January 1, 1986, is not eligible for the credit.

And where, you ask, is the good news? Well, depreciation, also known as the Accelerated Cost Recovery System, will provide for a more accelerated rate. For most property, other than real estate, the current 150% double declining balance will be increased to 200%. For instance, a piece of equipment costing $5,000 and qualifying as five year property would get $750 deduction under the old rules and $1,000 under the modified ACRS.

And here's an added bonus. Although most of the effective dates are January 1, 1987, there will be a choice for depreciation. If the property was placed in service between August 1 and December 31, 1986 you may elect which rule you wish to apply.

Now for the bad news. The piece of equipment qualifying as 5-year property under the old rules may have to be classified as 7-year property under the new rules and, if it does, first year depreciation, even though computed at double declining balance, drops to $714. The reason for this is that while in the good old pre-1987 days most personal property fell into the 3 to 5 year class, the new rules provide for six classes ranging from 3 to 20 years. Under the new rules, cars and light trucks are bumped up from 3 years to 5 years to be fully depreciated and office funiture and fixtures from 5 years to 7 years. The biggest change is in the rules providing for depreciation of real property.

In the last five years, these have bounced around a bit from 15 to 18 to 19 year treatment. The new rules boost the cost recovery life to 27 and 1/2 years for residential rental property and 31 and 1/2 years for nonresidential real property. What's more, only straight line depreciation can be used to depreciate real property after 1986.

If by any chance, you are in the process of acquiring a building for the

FAU/FIU to Create International Trade Center

The Florida Small Business Development Center recently awarded monies to the FAU and FIU centers to create an International Trade Center. The ITC will assist emerging businesses to establish themselves in international trade and will provide timely information to firms already established. The territory the ITC serves ranges from the Florida Keys to Ft. Pierce.

The FAU/FIU International Trade Center is a pilot program which, we hope, will become a prototype for other international trade centers throughout the State. The ITC provides seminars, counseling and support services to its clients. If you'd like to be placed on the ITC mailing list, please contact Bill Musella at the International Trade Center, Florida Atlantic University SBDC, Building T-9, Boca Raton, Florida 33431. (305) 338-2273.

continued from page 2

just in case the difference creates additional tax. Tell that to your bookkeeper.

As far as tax strategies are concerned, remember that for any equipment of furniture and fixtures bought since July of 1986, you will have a choice between the old and new rules of depreciation.

Bear in mind that if too many (40 percent or more) of these acquisitions fall in the last quarter, they will be subject to special, limiting rules.

Re-examine meal and entertainment expenses with the idea that 20 percent of the cost will not be deductible after 1986. And remember the stricter requirements regarding the "clear" business nature etc.

Marginal rates for individuals will be lower than corporate levels. If you are incorporated you may want to consider switching to an S corporation, a partnership or sole proprietorship.

All in all, what with the additional record keeping for meals and entertainment, the Alternative Minimum Tax, and the new rules regarding inventory, it's a safe guess that even if it should happen to fall into a lower bracket, the small business will end up laying out the tax savings for additional clerical or accounting costs.

One word of comfort. If you're worried that some of the changes in the law, especially as they effect 1986, will result in an underpayment of estimated tax, rest easy. IRS says they will waive penalties if the underpayment is the result of The Act.

Special thanks to our author, Ms. Helen Hughes. Hughes is a member of the AICPA and FICPA. She is a Certified Public Accountant with Ward and Hughes, P.A. in Delray Beach.

Also our appreciation to Arthur Young Co. for permission to reprint the charts "Overview of the Provisions Affecting Business" and the Depreciation Schedule.

Readers interested in obtaining a copy of their booklet "The Tax Reform Act" should call or write Arthur Young, 501 S. Flagler Dr. Suite 400 in West Palm Beach, 33401 (305/655-7139 Mr. Zenga), or 1 E. Broward Blvd, #710, Fort Lauderdale, 33301 (305/523-8300, Mr. Fattal).

Internationally Speaking...

P.E.A.P.S Program to Begin Soon

The "Program for Exporters of American Products and Services ("P.E.A.P.S")" is a four part training program, which includes classroom instruction, hands-on experience in the import/export trade, help in applying for appropriate licenses, and one-on-one counselling to help your business succeed and to provide you with current information on help available through government and local agencies. We will also provide you with information about overseas markets. "Sounds great," you say, "but what is this going to cost me?" Not a cent. The new International Trade Center is looking for residents of Palm Beach and Broward Counties who want to learn the exporting trade.

You can participate fully in P.E.A.P.S. and continue working at your current job. Courses will be offered in the evening and/or on weekends. You can arrange your own hours with our participating Import/Export firms and set your own schedule with our counselors. We hope to complete all interviews by mid to late February. P.E.A.P.S. is scheduled to get in gear by mid-March, 1987. If you'd like more information about this program or about what the International Trade Center can do for you, write to Bill Musella c/o the Small Business Development Center, Florida Atlantic University, Building T-9, Boca Raton, Florida 33431. His phone number is 338-2272.

"Exporting High Tech" to be Subject of First Wellington Symposium

A business that can't keep up with a changing business economy is doomed to fail. This is especially true in international trade. Plummeting oil prices in the Middle East caused high unemployment in Texas. Diplomatic disaster in Iran and racial tension in South Africa dramatically affected the lives and fortunes of American investors in General Motors and Kodak. In order to help our international trade clients keep up to date on current developments and changes in the international marketplace, we are offering a series of symposia focusing on specific areas of concern and interest to the international trader. The symposia will be held at the Wellington Club, 12165 Forest Hill Blvd., Wellington, Florida. The phone number for the Wellington Club is 793-3100.

On Friday, March 27th, from 9:00 A.M. until 3:00 P.M., the International Trade Center will be offering the first symposium of the Wellington Symposia series, "Exporting High Tech." Several presenters will discuss federal restrictions, world markets for the high tech trade, and recommended items for export. A light breakfast and a gourmet lunch will be served. Guests may choose one of two entrees. Reservations may be made by calling any FAU SBDC office (Boca:338-2273, Palm Beach Gardens: 627-4278, or Ft. Lauderdale: 355-5211). Reservations must be made prior to Friday, March 20th. Cost for the entire day is $20 per guest. For more information, write to Bill Musella c/o Small Business Development Center, Florida Atlantic University, Building T-9, Boca Raton, Florida 33431. His phone number is 338-2272.

Prepared Statement of Daniel Bailey, President, Rochester Gear, Inc., Rochester, NY, on Behalf of National Tooling & Machining Association

Mr. Chairman and members of the Committee. My name is Dan Bailey and I am President of Rochester Gear, Inc. in Rochester, New York. Our company and the estimated 12,000 other small companies in our industry form the foundation of the United States' industrial base. Our highly skilled workers produce molds, dies, precision machined parts, special machines and other tooling essential to modern mass production. We use increasingly sophisticated and costly computer aided design and computer aided manufacturing, or CAD/CAM machine tools.

We share several other characteristics with other manufacturing industries. First of all, our member companies are typically small, around 15 or 20 employees. In fact, most manufacturers in this country are small.

We share other characteristics with other manufacturing industries dominated by small businesses. We are internationally competitive. For virtually every small U.S. manufacturer there is not and never has been any such thing as a monopoly or an oligopoly. For my company and tens of thousands of other small manufacturers there never has been any lack of competition or any place to hide for those that can't compete domestically or internationally. We accept this competition as healthy for the industry -- making us stronger and more efficient. Despite a self correcting system which has assured international competitiveness and efficiency in this country since the dawn of the industrial revolution, just about every small manufacturer in this country has abruptly found his company undercut by predatory pricing by his foreign competitors in the last few years.

Virtually all small U.S. manufacturers are now being injured by unfair foreign competition and there is nothing we can do about it. The cost of bringing a case before the International Trade Commission can easily exceed several hundreds of thousands of dollars, more than the liquidated value of many of those companies. Unlike their larger counterparts, a small manufacturer does not have the option of moving his plant to a foreign country to take advantage of existing subsidies, low wages and so forth.

The reward for succeeding in a proceeding before the International Trade Commission is a duty imposed on the offender and paid to the government. The duty is prospective and not imposed if the party ceases its unfair trade practices in the future.

From the viewpoint of our foreign competitor, it is a "no lose" situation. They may not get caught and if caught, a good trade counsel may win the case for them. If they lose, they can still cease taking advantage of the cause of the fine in order to avoid penalty. It must be kept in mind that the level of penalties is so low that in most cases even this is not a deterrent.

Adding further insult to this situation, we find that the U.S. government is actively encouraging this process. Federal procurement practices are currently exempted from commercial trade law. This has allowed several agencies, in particular the Department of Defense, to knowingly purchase foreign sourced products at prices that are genuinely below market levels. Yet, the U.S. manufacturer has no recourse to defend himself.

There are two perspectives of small U.S. manufacturers. The very small U.S. manufacturer is powerless. The net worth of the company is not great enough to fund the necessary legal action. A larger small manufacturer might be able to borrow the money necessary to pursue the case, but those costs would find their way into increased product price, regardless of the outcome of the case.

To give you an idea of the impact, the average firm in our industry in 1985 had 39 employees, with an equipment investment of $25,000-70,000 per employee, $3.98 million in sales and a 4.9% pre-tax profit. To add perhaps a half a million dollars in burdensome legal fees, or about 12% of total sales, effectively closes off the litigation option for small manufacturers. For some import-impacted sectors, such as the gear industry, pre-tax profits were only about 2%.

We have several specific recommendations for your consideration.

First, we suggest that a Small Business Trade Law Advocacy Program be established within the SBA Office of Advocacy. That program would assist small businesses which have suffered as a result of foreign competition. It would be directed and funded to conduct such research as necessary as to determine the degree of impact and whether foreign practices illegal under the General Agreement on Tariffs and Trade had taken place.

In situations where the research indicated both injury and unfair foreign competition, the Office, which would include trade counsel, would be required to provide any and all such support as necessary to pursue the appropriate remedy through the appropriate U.S. or foreign administrative or judicial bodies.

Secondly, we suggest that Congress strengthen the private right of action provision for unfair trade practices which was enacted by Congress in 1916. Like other provisions of law of participating nations existing before the negotiation of the GATT agreement in the 1940's, this provision is grandfathered. The 1916 law is antiquated and needs revision to be an effective vehicle of recourse. If it were modified to apply to small business, it would at least allow a small company to recover compensation from the party causing the injury. Small companies, as risk takers, might be willing to take the risk of bringing legal action if they knew they had a chance of recovering their costs and receiving compensation for their injury.

A private right of action provision was in last year's House-passed trade legislation, in H.R.3 this year, and is being considered by the Ways and Means Committee at this time in connection with a multiple offender dumping provision.

Our third proposal is aimed at the diversion that is likely to be caused by the imposition of large dumping or countervailing duties. In such cases, we believe that it is reasonable to expect administering authorities to be alert for the possibility of diversion.

Our proposal would require monitoring of increases in imports of downstream products that are likely to be vehicles for diversion. Where large (15% or more) dumping or subsidy duties have been imposed on input products such as steel -- or where a restraint agreement is used to settle a dumping or subsidy case involving large (15% or more) preliminary determinations of unfair trading -- U.S. producers would be able to identify to the Commerce Department other products in which the dumped or subsidized output is likely to be used as a major part, component or material. Commerce would refer lists of those downstream products meeting the statutory test to the International Trade Commission which would monitor imports of those products. If this system were in place, it might detect what we believe is diversionary dumping within the tooling industry. We believe that this diversionary dumping is occurring in a number of niche markets in the tooling industry. We are presently seeing 15 to 20% reductions in pricing of foreign sourced gearing products, even with the major shift in exchange rates that has occurred with key trading partners.

In the event imports of monitored downstream products from a foreign country increase by more than 5% in any quarter, the ITC would analyze the increase and give public notice of its findings. Thereafter, the Commerce Department could investigate whether there was dumping or subsidization of components, and private industry could initiate an appropriate trade case.

As I mentioned, federal agency procurement is currently exempted from trade law, allowing known violations to go undeterred. If this Congress were to lift that exemption, allowing trade remedy cases to be filed where bona fide evidence exists that a foreign source product was purchased at below market prices, small business would be able to address this serious grievance.

Lastly, Section 232 of the Trade Expansion Act of 1962 allows for cases to be brought -- and relief to be granted -- due to imports that threaten U.S. national security. We believe that surging imports of vital manufactured products poses a growing threat to America's national security. This makes it especially important that petitioners in Section 232 cases be given the certainty of timely government responses. At present, however, there are no strict time limits on Presidential decision-making in such cases. For example, in the Section 232 petition filed by the National Machine Tool Builders Association in March 1983, it took more than three years to get a Presidential decision (to pursue machine tool VRAs with major foreign suppliers). As a result, during those three years, imports continued to wreak untold damage on an industry vital to the U.S. defense base.

If anything, the tooling and machining industry is more important to the U.S. defense industrial base. During WWII the small companies in our industry had no choice but to shift from a mostly commercial market to an almost totally defense market overnight. Without the tooling we supplied to our defense aviation, naval and ordnance industries, our country would not have been able to out-produce Germany and Japan combined by a 2/1 ratio in many categories of defense hardware. Sadly, that U.S. surge production capability no longer exists.

Congress should -- at minimum -- impose a strict time deadline on decisions by the President in Section 232 cases. We therefore, support H.R.3's shortening of the Section 232 time line for decisions by the Secretary of Commerce. However, we urge Congress to review, and give further guidance on, the list of factors the Executive Branch should consider in making determinations under Section 232, e.g., whether negative determinations should be allowed based on the fact that surging imports come from U.S. allies as was the situation in the 232 petition brought by the U.S. fastener industry.

With respect to other trade related issues facing the committee, we believe that the first step to U.S. export enhancement is the elimination of unfair foreign trade practices. Healthy small companies who are competitive in their own country have a natural inclination to use excess available resources to expand into foreign markets. Weakened small companies, who find themselves at a disadvantage in their own markets have neither the time, money or resources to waste in futile efforts to compete with those same foreign companies who are significantly undercutting their prices in their own markets.

This does not mean that even in the present environment some export opportunities do not exist. Our industry has funded its own efforts to develop potential relationships with the People's Republic of China. Members of the association have had official visits in China with potential Chinese customers and they have sent representatives to the U.S. to visit with us. We have to act quickly when such opportunities present themselves. We can't afford to wait for a time consuming screening process in the Department of Commerce to determine whether we can get support for such an effort.

If you want to help small business develop export markets, you must develop a system within the Commerce Department or S.B.A. which is flexible and not cumbersome. It must consist of processes which can evaluate new and innovative approaches in a timely manner, and allocate support, if needed, in an appropriate and timely manner.

Small businesses were dealt a severe setback in their ability to compete domestically and internationally by the 1986 Tax Reform Act. The repealed 10% investment tax credit often enabled cash strapped small businesses to use money which would otherwise have been sent to IRS in their next quarterly tax payment to make a downpayment on an expensive machine tool so that they could accept new business. Today, that same company will not be able to accept that work, buy that equipment, or hire the workers needed to run it.

With respect to technology diffusion, the most notable barriers to acquiring and applying new technologies are reduced incentives for capital formation, and research and development as well as misdirected government trade and procurement policy. Small business has always produced more than its share of technology. Today, it is foreign governments which are offering their businesses the best package of incentives to produce new technology, and those businesses are responding. Give us the same incentives and we will respond in the same manner.

Federal procurement policies have also been misdirected. We estimate that only 10% of the $22 billion dollar DoD annual purchase of spare parts is through the process of formally advertised sealed bids. Much of it cannot be competed because the data is proprietary to large corporations. Failure of the Defense Department to purchase data not only restricts the size of the U.S. defense industrial base by precluding our members from bidding, it also restricts the diffusion of the new technology that is required to produce those parts. Since open competition also saves nearly 50% on spare parts purchases, increasing competition in this area would help reduce the deficit at the same time it helps expand the size of the defense industrial base and diffuses technology. We strongly urge the Committee to seek means of increasing competition in defense spare parts procurement. We would be happy to offer suggestions on how that could be achieved.

Thank you for the opportunity to visit with you today. Small businesses continue to be bankrupted by unfair foreign competition while the large U.S. corporations that are often our customers go offshore. In the interest of maintaining a strong U.S. industrial base and defense industrial base, we urge you to develop a strong and aggressive small business trade title.

PRESS RELEASE

NATIONAL TOOLING & MACHINING ASSOCIATION
9300 livingston road, ft. washington, md. 20744 • phone 301-248-6200

For Immediate Release

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NTMA CALLS FOR EFFECTIVE TRADE REMEDY FOR SMALL U.S. MANUFACTURERS

(Washington, D.C. - March 25, 1987) ... Speaking on behalf of the many small manufacturers impacted by unfair foreign competition, NTMA member Dan Bailey urged the House Small Business Committee to develop a strong and aggressive small business trade title which would include remedies such as a private right of damages and a Small Business Administration Office of Advocacy.

In the March 25 testimony, Mr. Bailey, President of Rochester Gear, Inc., Rochester, New York, told committee members that, "Virtually all small U.S. manufacturers are now being injured by unfair foreign competition and there is nothing we can do about it. The cost of bringing a case before the International Trade Commission can easily exceed a half a million dollars, more than the liquidated value of many of those companies."

"The reward for succeeding in a proceeding before the International Trade Commission is a duty imposed on the offender and paid to the government. The duty is prospective and not imposed if the party ceases its unfair trade practices in the future.

"From the viewpoint of our foreign competitor, it is a no lose situation. They may not get caught and if caught, a good trade counsel may win the case for them. If they lose, they can still cease taking advantage of the cause of the fine in order to avoid penalty.

"There are two perspectives of small U.S. manufacturers. The very small U.S. manufacturer is powerless. The net worth of the company is not great enough to fund the necessary legal action. A larger small manufacturer might be able to borrow the money necessary to pursue the case, but those costs would find their way into increased product price, regardless of the outcome of the case."

Mr. Bailey made several specific recommendations for the Committee's consideration:

First, that there be established within the SBA Office of Advocacy, a small business trade law advocacy program. That program would assist small businesses which have suffered as a result of foreign competition. It would be empowered and funded to conduct such research as necessary as to determine the degree of impact and whether foreign practices illegal under the General Agreement on Tariffs and Trade had taken place.

In situations where the research indicated both injury and unfair foreign competition, the Office, which would include trade counsel, would be required to provide any and all such support as necessary to

-more-

pursue the appropriate remedy through the appropriate U.S. or foreign administrative or judicial body.

Secondly, that the private right of action provision for unfair trade practices which was enacted by Congress in 1916 be strengthened. This law allows businesses to sue foreign competitors for the damages caused their business by unfair trade practices. Like other provisions of law of participating nations existing before the negotiation of the GATT agreement in the 1940's, this provision is grandfathered. The 1916 law is antiquated and needs revision to be an effective vehicle. If it were modified for small business, it would at least allow a small company to receive compensation from the party causing the injury.

The third proposal is aimed at the diversion that is likely to be caused by the imposition of large dumping or countervailing duties. In such cases, NTMA believes that it is reasonable to expect administering authorities to be alert for the possibility of diversion.

The proposal would require monitoring of increases in imports of downstream products that are likely to be vehicles for diversion. Where large (15% or more) dumping or subsidy duties have been imposed on input products such as steel -- or where a restraint agreement is used to settle a dumping or subsidy case involving large (15% or more) preliminary determinations of unfair trading -- U.S. producers would be able to identify to the Commerce Department other products in which the dumped or subsidized output is likely to be used as a major part, component or material. Commerce would refer lists of those downstream products meeting the statutory test to the International Trade Commission which would monitor imports of those products.

In the event imports of monitored downstream products from a foreign country increase by more than 5% in any quarter, the ITC would analyze the increase and give public notice of its findings. Thereafter, the Commerce Department could investigate whether dumping or subsidized components, and private industry could initiate an appropriate trade case.

Lastly, Section 232 of the Trade Expansion Act of 1962 allows for cases to be brought -- and relief to be granted -- due to imports that threaten U.S. national security. NTMA believes that surging imports of vital manufactured products poses a growing threat to America's national security. This makes it especially important that petitioners in Section 232 cases be given the certainty of timely government responses. At present, however, there are no strict time limits on Presidential decision-making in such cases.

NTMA, composed of over 3,400 member companies throughout the U.S., is the national representative of the $20 billion a year applied technology industry. Without the service of this industry, modern mass production would not be possible. Member firms contract to design and manufacture tools, dies, molds, gages, special machines, and provide precision machining services to virtually every other manufacturing industry. Among customer industries are the automotive, aerospace, agriculture, chemical, home appliances, electronics, energy, and defense-related industries.

Founded in 1943, NTMA is proud of 43 years of service to American industry.

[illegible]

Four Vital Industry Components

[illegible]

National Tooling &
Machining Association

NTMA

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

National Tooling and Machining Association
9300 Livingston Road, Ft. Washington, MD 20744

THE ROLE OF THE MEMBERS OF THE NATIONAL TOOLING AND MACHINING ASSOCIATION IN THE MANUFACTURE OF AMERICAN PRODUCTS

The National Tooling and Machining Association (NTMA) represents the contract tooling and machining companies located in the United States.

Virtually all of the 12,000 companies in the industry are small businesses. Yet, the industry generates sales in excess of $20 billion a year. The 125,000 engineers, skilled toolmakers, diemakers, moldmakers, and machinists employed in the industry design and manufacture tools, dies, jigs, fixtures, gages, special machines, and precision machined production parts. Some firms specialize in experimental research and development work.

Employment in these companies ranges from less than ten to more than six hundred persons, with the average being about twenty skilled employees. The majority are privately owned and operated.

This tooling and machining industry is the backbone of modern mass production and produces much of the manufacturing technology and know-how exhibited in the United States. Nearly every manufacturer does business at one time or another with the contract tooling and machining industry. It supplies the necessary precision tooling and machining for such vital industries as defense, automotive, aerospace, appliance, business machines, electronics, agricultural implements, ordnance, transportation, environmental, construction equipment, nuclear and many more.

NTMA has chapters in 65 industrial areas throughout the United States. The bulk of the Association's activities are in support of NTMA's five major aims. These aims are:

- To assist the membership in remaining competitive by developing, improving, and expanding its markets, both foreign and domestic;
- To promote continuing education in application of management principles;
- To develop a comprehensive structure for training on all levels;
- To represent its members and industry in relationships with government; and
- To publicize the services of the industry and the Association to all their various publics.

National Tooling and Machining Association
9300 Livingston Road, Ft. Washington, MD 20744

Prepared Statement of Hon. Leanna Brown, State Senator, State of New Jersey

New Jersey Senate

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WEDNESDAY, MARCH 25, 1987

I am New Jersey State Senator Leanna Brown, a member of Governor Thomas H. Kean's Commission on International Trade and Vice-Chairman of Congressman Dean A. Gallo's Small Business Export Opportunity Task Force. I am pleased to offer my comments at your hearing. Today there is a dark cloud on our nation's economic horizon in the shape of the $170 billion trade deficit. At a recent meeting in New Jersey, the trade deficit was referred to as a hidden national crisis; hidden, because the imbalance in trade has little significance to the average American, for the intricacies of international trade are understood by few, and crisis, because our standard of living will suffer if we continue to lag behind other nations in aggressively selling our products abroad while consuming vast quantities of foreign made goods.

Historically, the United States has not been a nation dependent on trade. Unlike the British, Dutch and Japanese, the size and resources of the United States created vast business opportunities within our borders. When times have been good, business sees no need to trade abroad, and when times have been bad, the essential groundwork necessary for international trade has not been undertaken and "instant deals" are rarely possible. Patience and persistence are essential.

There is a crying need to build a constituency for international trade in the United States. For every billion dollars worth of exports, 25,000 Americans are employed. The White House Conference on Small Business ranked trade high in its list of priorities. The visibility your committee is giving to the importance of trade for small and medium business is most laudable. Many large corporations could also be more aggressive in gaining international business for American workers. Historically, government assumed Big Business knew its way around internationally and therefore government focused its assistance on smaller businesses. I question that assumption.

There is no quick fix to the trade imbalance. In a global economy the United States must be competitive. Our corporations, large and small, must be well run and eager for business. The day and age of the John Wayne "go it alone" hero as he conquers the "new frontier" in the United States is over. Changes in the the world require a public-private partnership rather than the big stick approach that President Theodore Roosevelt used. Government can be most helpful in the international arena. American business must realize the advantage of interacting with government, labor and the academic world, for example, to maximize its product for sale in the world marketplace.

In my time before the committee I would like to outline how I became involved in trade, what the state of New Jersey is doing, the trade initiatives of my Congressman Dean A. Gallo and suggest how the federal government could help small business in the global economy.

Like many Americans in the 1940's and 1950's I spent time in the public school classroom learning about other parts of the world and studying foreign languages. I went on to major in government, with an emphasis on international relations, at Smith College in Massachusetts and graduated in 1956. At Educational Testing Service in Princeton, I wrote questions for the State Department's foreign service examinations. Participating in programs like the Experiment in International Living I have enjoyed travelling abroad and entertaining foreign visitors in New Jersey.

In 1983 my husband, an AT&T employee, and I took our second trip around the world. We talked with business and embassy officials in the Far East and Saudi Arabia. As I result of the trip, I introduced a package of bills in the New Jersey Legislature. One of them was the establishment of the New Jersey Commission on International Trade and I am pleased to serve on that Commission. As a member of the Revenue, Finance and Appropriations I have also been successful in increasing the budget for New

Jersey's Division on International Trade which is in our Department of Commerce and Economic Development.

Last November we again travelled to the Far East and this time included Seoul as well as Tokyo and Singapore. We made our first visit to India and Frankfurt. In each country we talked with American business people and representatives at the U. S. Embassies. They shared a strong concern with the lack of American business presence in their countries. In contrast to foreign firms who come to New Jersey knowing our customs, our geography, our business climate and an understanding of what is needed in the market place, Americans do not do similar homework. Instead, they want government and chamber of commerce representatives to find them a partner for a joint venture. They expect business inquiries to come to them rather than aggressively seeking business abroad.

Government will never be able to do the leg work for small business which needs patience, persistance and knowledge to compete internationally. However, government can help with information and training.

In New Jersey, trade receives bipartisan support. Under the leadership of Governor Kean the Division of International Trade has flourished. Strong support has come from the legislature which is controlled by the Democrats in the Senate and the Republicans in the Assembly. Trade must come before partisan politics.

There is a strong role for the states to play in trade. We are particularly geared to help small business. In his State of the State Message in February, Governor Kean gave trade top priority. In 1986 he personally visited the Far East, one of 67 gubernatorial missions abroad last year. New Jersey is seeking to establish a trade office abroad as have 36 other states.

International trade is a two way street. New Jersey is most successful in attracting foreign firms, which provide jobs and contracts for small businesses as one of its positive spinoffs. We rank fourth in the amount of foreign investment and tenth in the value of goods exported--$8.38 billion.

In addition to the New Jersey Commission on International Trade, which includes among its members legislators of both parties and outstanding representatives of the business community, we have two port authorities, the New York/New Jersey and the Delaware River, which have extremely effective trade operations. X-port, a trading company under the auspices of the New York/New Jersey Port Authority, has helped many small businesses get into exporting.

In December, Congressman Dean A. Gallo held a trade seminar for small businesses in his district in New Jersey. Representatives from both state and federal agencies directly involved with trade and small business addressed a wide variety of problems. Also included were "how to" workshops to answer specific questions. It was an excellent example of federal-state cooperation to address a national priority, increased exports. Representatives from state government gave specific advice on tapping the foreign market.

Following on this most successful and oversubscribed event, the Congressman established the Small Business Export Opportunity Task Force to zero in on specific areas of improvement necessary to increase exports by small business. The fact that 85% of exporting is done by only 380 firms in the United States is of concern. At its first meeting in February the observation was made that when large firms increase the amount of trade small firms are also given increased export oppurtunities. The task force recommendations should be forthcoming this year.

How can the federal government help small business in the global economy? From my extensive experience, I believe that there are a number of ways we can take positive action to help small businesses increase their exports. I have shared these ideas with Representative Gallo's Task Force and am pleased to share them with you.

1. Establish a Department of Trade which will coordinate and oversee the United States's participation in the world marketplace.

2. Establish an export hotline to provide a centralized data base, accessed through designated state agencies.

3. Increase trade fair participation by expanding the Foreign Trade Fair Certification Program, providing assistance before, during and after shows and expanding the Foreign Buyer Program.

4. Institute trade agreements which deal with services as well as products.

5. Encourage worldwide agreements to respect intellectual property and patent protection.

6. Remove disincentives for trade. It is important the United States is only as strict as competing nations, for example, in the area of issuing export licenses.

I appreciate the time you allowed me to share my thoughts on small business and international trade. If the United States is to remain a viable participant in the world economy we must give our businesses the knowledge and incentives they need to be the best.

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PREPARED STATEMENT OF JOHN F. CICCARELLI, STATE DIRECTOR, MASSACHUSETTS SMALL BUSINESS DEVELOPMENT CENTER

Thank you Mr. Chairman for the opportunity to testify before you today. I wish to commend you for working with the House Leadership to incorporate a small business title in the trade bill to be considered soon by the full House. For the record, my name is John Ciccarelli. I am the State Director of the Massachusetts Small Business Development Center program and also immediate Past President of the Association of Small Business Development Centers. My office is located at the School of Management at the University of Massachusetts in Amherst.

Over the past several weeks, in this Committee's hearings on the Administration's FY 88 budget proposal and in hearings on international trade, you have heard testimony both pro and con, regarding the Small Business Development Center program. I would like to begin my testimony by dispelling several notions with regard to the SBDC program nationally.

The first is that academic involvement is inappropriate to serve small business. I would like to provide several illustrations why this notion is false.

When one looks at the enormous change in the economy in Massachusetts, clearly one of the most important partners in that change has been academia. The Route 128 belt and the new Route 495 belt have been developed in part because of the very strong tie to the academic infrastructure which we have in our state. The role our educational institutions have played in the overall economic development strategy in our state has been heightened and continually supported through our Center of Excellence program which links government, universities and the private sector to jointly develop technology in certain defined areas i.e., microelectronics, polymers, bio-technology, marine science and photovoltaics created by Governor Michael Dukakis. The payoff of this partnership relationship is that technological breakthroughs are carefully nurtured to the point of commercial application.

It is likewise inappropriate to say that because SBDCs are located at universities they will not and cannot service the needs of small business. I submit that university-based SBDCs are servicing the needs of small business far better than any other program that has been established to date. The reason is not because they are set in academic environments, but because they function in a partnership environment. Congress had great foresight when it demanded that the SBDCs function as a partnership and that requirement has now resulted in the creation of an effective small business assistance network.

A partnership has to be constructed with care. None of the partners to a program, be they the federal or state governments, or the academic hosts or the private sector, can be allowed to have undue influence or it will quickly become unproductive. However, when there is a balanced relationship, which on the whole is what has occured in the SBDC program, then the possibilities become endless in the ways in which small business can be assisted.

Critics have charged that our counseling and training is done primarily by faculty and graduate students. Nothing could be further from the truth. We do use faculty and graduate assistants, but in a very controlled environment, working along side full-time consultants and in many cases working hand-in-hand with private sector consultants, to bring the best possible assistance to small business.

In addition, our counselors, many of whom are full time, have significant business expertise. They have either owned or operated their own businesses or held responsible jobs in major corporations. Many of these people are now in a position to enjoy the fruits of their labors, but at the same time they have a desire to give something back to their communities. To our delight, they have found the SBDC to be a highly appropriate vehicle for providing community service by sharing their knowledge and expertise with all kinds of small businesses.

These individuals are backed up by MBA graduate students who work in concert, and under the direct supervision of, the counselor. For example, they do market research and help program our computers so we can better serve our clients. When specific problems arise which may be beyond the expertise of our own counselors, we are able to call on faculty, who are carefully screened to make certain they understand and relate to the needs of the small business owner. In addition, we continually look to the private sector to help us deal with very specific problems. This assures our providing the best possible assistance to small business and at the same time fosters the partnership nature of the program.

To illustrate, I have included as part of my testimony a chart showing the work experience of the state SBDC directors. It was created from information obtained in 1985. We are presently updating this information and with your permission will submit additional data for the hearing record.

I would like to briefly give you examples of specific work experience of a few SBDC directors. The Maine SBDC Director was formally an investment banker on Wall Street. The South Carolina Director has twenty years of senior banking experience. The Oregon Director had senior management experience with the Xerox Corporation. And, I worked for fourteen years in economic development first with the Massachusetts State Office of Minority Business Assistance and then as the first Deputy Commissioner for Small Business Assistance.

Besides the private sector work experience of our directors, the table shows that as much as 70% of an SBDC's counseling and 90% of its training is delivered by the private sector. In Massachusetts, 64% of our training instructors have private sector backgrounds. In absolute terms, 192 of our 292 trainers have had private sector careers. Only by leveraging the resources provided by the SBDCs can these private consultants afford to work with smaller clients who otherwise could not

SBDC	Directors Education Graduate Degree		Directors Years of Private Non-Academic Sector Experience	Percent of SBDC Counseling Delivered thru private source (cost reimbursement basis)	Percent of SBDC Training Delivered thru private source (cost reimbursement basis)
	Yes	No			
Alabama	X		5 (management)	10% (30%)	50% (0)
Arkansas	X		3 (CPA)	0	50% (10%)
Connecticut		X	35 (management)	10% (5%)	90% (10%)
Florida	X		2 (manufacturing)	15% (1%)	65% (5%)
Georgia	X		4 (management)	30% (10%)	65% (50%)
Illinois		X	9 (management)	42% (20%)	40% (15%)
Iowa	X		2 (management)	53%	53% (80%)
Kansas	X		7 (management)	50% (95%)	70% (85%)
Kentucky	X		21 (management)	10% (10%)	80% (10%)
Louisiana	X		28 (management)	25% (2%)	15% (0)
Maine	X		15 (management)	10% (100%)	25% (100%)
Massachusetts	X		9 (management)	10% (9%)	64% (58%)
Mississippi	X		12 (management/industrial development)	10% (100%)	25% (80%)
Missouri	X		20 (management/business owner)	20% (5%)	65% (15%)
Nebraska	X		3 (technical/journalist)	30% (90%)	25% (80%)
New Jersey	X		4 (technical)	20% (20%)	10% (80%)
New Hampshire	X		3 (management)	10% (5%)	50% (50%)
New York	X		5 (management)	10% (2%)	20% (8%)
Oregon	X		5 (management)	40% (10%)	90% (50%)
Pennsylvania	X		5 (management)	5% (0)	76% (0)
Rhode Island		X	7 (technical)	70% (90%)	40% (50%)
South Carolina		X	20 (management)	7% (65%)	48% (97%)
Tennessee	X		16 (management)	13% (10%)	90% (2%)
Texas (Houston)	X		15 (management)	30% (10%)	60% (50%)
Utah	X		10 (management)	15% (13%)	30% (25%)
West Virginia	X		20 (management)	10% (0)	40% (0)
Wisconsin	X		12 (management)	30% (25%)	50% (40%)

afford their services. However, as they grow and expand, these companies can afford and will seek out assistance from private sector consultants on a fee basis.

What we are seeing in Masschusetts is that private sector consultants have become a tremendous referral network for us and we have become an equally important referral service for them. As more and more accountants, management consultants, and lawyers learn about our program, they refer an increasing number of clients to us. Hopefully, this experience, which is representative of SBDC experience across the country, will help dispell the second erroneous concept about the SBDC program -- that we are in competition with the private sector. The truth is, since we are not charging fees and are only helping those small businesses which can least afford to pay for our kind of help, we not only do not compete with, but actually develop increased business for private consultants as the client grows and prospers.

Having briefly addressed some of the arguments of our critics, let me discuss how we can help insure that our domestic economy remains strong and we once again become competitive in the international marketplace. First and foremost, there is a great deal of education and assistance needed to bring our small businesses to a point where they can create new technological advances and in turn bring them into commercial application in both domestic and international markets. I can think of no better way to begin that process than through the SBDC program. With 49 SBDCs now located in over 600 cities and towns, we have created a tremendous network linking schools of engineering, business, law, and the other resources of universities. We believe large amounts of these types of important resources can help newer, younger small businesses become competitive in international trade.

For example, one of the issues affecting today's manufacturers is quality control. We are hearing from more and more major corporations that their primary concern with their small subcontractors and vendors is quality. The Massachusetts

SBDC (MSBDC) is in the formative stages of addressing this issue. The University of Massachusetts was contracted by a major auto manufacturer to develop a Statistical Process Control System for one of their plants. The SBDC has now been asked to work with those who have advanced this process and to refine it to the meet the needs of smaller manufacturers and use a network including the MSBDC to provide training and on-site counseling.

This is a stellar example of how our SBDC has been able to take advantage of being in a university setting. Without this university affiliation, the opportunity to bring a state of the art quality processing to small businesses would have undoubtedly been missed.

One of the issues which the Committee should pursue is how can the technology and expertise which exists in university engineering and computer program departments be linked with small businesses to bring innovative ideas more rapidly to commercialization. The SBDC is well positioned to provide such a service because not only is it the link to technology from our engineering schools, but it can also provide management assistance, marketing, production and financial advice which early growth companies desperately need. Having said this, we must be cognizant of the fact that quality engineering programs are in great demand and large corporations are providing significant financial support to obtain this expertise.

Our SBDC program has been able, from time to time, to link technological advances to small business clients. For example, one of our clients yesterday spent a half a day with members of the University of Massachuetts polymer science center to discuss the possibility of providing technical assistance for manufacturing their particular product. The item is a component extensively used by the elderly and physically disabled. However, greater financial resources are needed if we are to provide a more meaingful technology linkage to a greater number of smaller businesses.

Once this technology linkage is in place, there must also be available a source of funding for these small businesses. In Massachusetts, we are fortunate to have over a dozen quasi-public financing programs which can be used to leverage other public and private financing sources. However, these programs are only effective if there is a coherent business plan and a solid approach to managing the company. New technology firms need significant education and coaching to understand and attract financing. Older firms are also looking to upgrade their processes or develop new product lines. They often need extensive assistance for they are usually entering into market and financial areas unfamilar to them. For this reason, the MSBDC participates in the monthly meetings of the quasi-public finance agencies to insure that quality management assistance is made available to applicant businesses. Our Capital Formation Service is specifically designed to assist smaller businesses pursuing not only state and municipal sponsored financial assistance, but specialized federal loan programs such as the SBA's 503/504 loan program, SBIC program, and 7(a) loan program. Private venture capital is also utilized. To determine which financial avenue to pursue, we provide a complete analysis of all options and identify the one we believe to be most appropriate. To date, our Capital Formation Service center alone has helped secure over $31 million for small businesses through a variety of sources. In FY 86, 47 percent of the clients were manufactureres of both low and high tech products. Our other five regional centers have channeled $44 million to small firms which have created 2,500 new jobs.

In conclusion, collaboration of all partners is critical in enabling small businesses to obtain quality management and technical assistance. The educational community has played an indispensable, critical role in this economic development process. The ability to link more small businesses with educationally sponsored resources will enhance their ability to develop new products and cost effective services.

The SBDC program is clearly a model for a government, educational and the private sector partnerhip. Yet, SBDCs have only scratched the surface in what could be made available if additional resources were made available to the program.

MASSACHUSETTS SMALL BUSINESS DEVELOPMENT CENTER

ACHIEVEMENTS OF 1985 - 1986

Total Clients Served:	2,902
Total Hours of Counseling Provided:	24,563
In-Depth Clients: (receiving 12 hours or more)	699
Total Hours Provided In-Depth Clients:	19,027
Female Clients:	987, 36% of total
Minority Clients:	380, 13% of total
Financing Secured:	$19,216,700
Jobs Created:	585 Full-time 20 Part-time
Jobs Retained:	308 Full-time 6 Part-time
Total Training Programs Provided:	198
Attendees:	3,586

ACHIEVEMENTS 1980 - SEPTEMBER 29, 1986

Total Clients Served:	12,385
Total Training Programs Provided:	779
Attendees:	19,646
Financing Secured:	$74,145,550
Jobs Created:	2,305

ECONOMIC IMPACT

Three impact surveys of clients receiving 5 hours or more of counseling and whose cases were closed for a minimum of one year revealed the following:

75% increased sales
58% increased profits
38% increased employment
3,151 new jobs created
$15 million in tax revenues generated

J18/3/6/B

SBDC SURVEY RESULTS

SBDC Name	State Directors Years in Private Sector	State Directors Private Sector Work Experience	% SBDC Counseling Through Private Source	% SBDC Counseling Cost Reimbursement Basis	%SBDC Training Through Private Sector	%SBDC Training Cost Reimbursement Basis	Number of Private Sector Consultants Provided Counseling/Training
Alabama	4	Management Technical	5	2	50	5	75
Alaska	6	Marketing	15	15	15	15	N/A
Arkansas	9	CPA, Auditor	None	None	50	2	200
Connecticut	30	Management	15	2	15	1	85
Delaware	10	Management	5	5	50	40	22
District of Columbia	7	CPA	25	0	20	0	250
Florida	2	Manufacturing	5	1	50	0	400
Georgia	4	Advertising	10	5	48	10	146
Idaho	15	Management	10	5	15	3	25
Illinois	10	Entrepreneur	12	90	35	90	25
Indiana	20	Management	90	0	100	80	8
Iowa	30	Management	37	37	35	35	160
Kansas	17	Management Marketing	27	25	26	19	122

SBDC Name	State Directors Years in Private Sector	State Directors Private Sector Work Experience	% SBDC Counseling Through Private Source	% SBDC Counseling Cost Reimbursement Basis	%SBDC Training Through Private Sector	%SBDC Training Cost Reimbursement Basis	Number of Private Sector Consultants Provided Counseling/Training
Kentucky	39	Management Accounting	10	N/A	~~116~~ 66%	~~66~~ N/A	116
Louisiana	23	Management	5	5	30	20	65
Massachusetts	14	Economic Development	10	98	72	67	263
Michigan	4	Management	9	5	20	10	40
Minnesota	8	Management	26	26	40	35	111
Mississippi	19	Management	5	5	40	30	32
Missouri	25	Marketing	40	15	90	10	425
Nebraska	8	Publishing Printing	10	10	25	18	21
New Hampshire	10	Attorney Management	5	3	60	40	12
New Jersey	5	Marketing	14	14	80	40	160
New York	7	Marketing Finance	5	8	40	5	100
Nevada	8	Marketing Management	30	28	60	40	200
North Carolina	15	Attorney Corp. Executive	5	less than 10	75	None	12

SBDC Name	State Directors Years in Private Sector	State Directors Private Sector Work Experience	% SBDC Counseling Through Private Source	% SBDC Counseling Cost Reimbursement Basis	%SBDC Training Through Private Sector	%SBDC Training Cost Reimbursement Basis	Number of Private Sector Consultants Provided Counseling/Training
North Dakota	17	Retail Management	0	0	20	7	2
Ohio	1	Market Research Consulting	95	8	95	8	25
Oklahoma	43	Technical Management	5	3	10	0	53
Oregon	5	Sales/Marketing	18	10	74	24	340
Pennsylvania	4	Management	14	10	75	0	80
Puerto Rico	10	Management Marketing	20	5	50	20	27
Rhode Island	5	Technical	83	75	85	30	75
South Carolina	21	Accounting Banking	2	2	23	23	35
South Dakota	14	Entrepreneur	5	4	50	30	12
Tennessee	19	Management Auditor	10.8	8	92	0	231
Texas (Houston)	15	Management	53	0	80	0	40
Texas (Northeast)	5	Management	N/A	N/A	N/A	N/A	N/A

SBDC Name	State Directors Years in Private Sector	State Directors Private Sector Work Experience	% SBDC Counseling Through Private Source	% SBDC Counseling Cost Reimbursement Basis	%SBDC Training Through Private Sector	%SBDC Training Cost Reimbursement Basis	Number of Private Sector Consultants Provided Counseling/Training
Texas (Northwest)	12	Management	N/A	N/A	N/A	N/A	N/A
Texas (South-Border)	13	Entrepreneur Management	0	0	50	10	5
Utah	13	Management Marketing	35	25	65	40	30
Vermont	10	Business Owner	8	8	20	10	10
Virgin Islands	16	Management Counsulting	15	10	40	0	50
Washington	15	Marketing Management	2	5	95	100	101
West Virginia	25	Management	5	0	15	0	75
Wisconsin	13	Economic Development	22	19	12	12	94
Wyoming	9	Management Sales	60	11	60	40	35

PREPARED STATEMENT OF SUSAN M. GARBER, STATE DIRECTOR, PENNSYLVANIA SMALL BUSINESS DEVELOPMENT CENTER

Mr Chairman, my name is Susan Garber and I am the state director of the Pennsylvania Small Business Development Center program. My office is located at the Wharton School at the University of Pennsylvania. I want to thank you for giving me the opportunity to testify before the Small Business Committee about trade and competitiveness issues for small business.

The Pennsylvania Small Business Development Center (PASBDC) network consists of thirteen university-based centers and sixty county outreach offices serving small businesses throughout the Commonwealth. The SBDCs throughout the state provide free one-on-one counseling in the basic operational and strategic areas of business management, such as business plan development, financing, marketing and advertising, accounting, product development, and long-range strategic planning. The SBDCs offer specialized assistance in business law, engineering, technology transfer, international trade, procurement, and R&D funding. Several of the areas of SBDC intervention listed above such as business law, engineering, and technology transfer will be addressed in more detail later in this testimony.

The SBDC provides low-cost seminars and workshops on an entire range of business-related topics and, because of its university affiliation, also conducts research on behalf of its clients and the local business community. Since the establishment of the SBDC network in 1979, it has provided business assistance and training to approximately 69,000

Pennsylvanians. In 1986 alone, over 9,000 people attended training seminars and more than 6,000 small business clients received individual counseling.

I could continue for the entire ten minutes alloted to me detailing the activities of the Small Business Development Centers, but I have been asked to focus this testimony on several specific issues. I will use my time before this committee to explore some of the competitive problems and opportunities which have confronted Pennsylvania small and mid-size companies in a newly-competitive economic environment. I will then speak to several initiatives which have been undertaken in the Commonwealth to increase the success potential of these companies.

To cite the recent Pennsylvania Business Roundtable report, Pennsylvania has undergone a gradual transformation during the last 30 years from an economy built on farm, mine and factory to an economy now confronted by global forces which demand high productivity, low production costs, high capital-intensity, low labor use, and different and fewer raw materials. Many of the single-industry communities in the state have lost their principle employment and revenue base while much of the manufacturing base of the central part of the state has been greatly diminished. Clearly, much of this revenue base has been replaced with service-sector firms, but it would be naive to believe that a healthy economic environment can be created with the emergence of a purely service economy. Rather, Pennsylvania needs to develop a diverse economic base which will not be dependent on a single measure of economic success or strength.

One of the primary initiatives undertaken in Pennsylvania in the last two and a half years is the establishment of the Ben Franklin Partnership programs. In an effort to lessen the Commonwealth's susceptibility to the vicissitudes of its traditional industries, the Ben Franklin Partnership has encouraged the diversification of the state's economies by creating four Advanced Technology Centers each of which has selected three or four areas of research in which to concentrate development efforts. The Ben Franklin program has capitalized on the strengths of its affiliated institutions and has tried to develop the economic strengths of the regions served by each Advanced Technology Center. For example, the Northeast Tier Advance Technology Center, based at Lehigh University, specializes in CAD/CAM, polymers/materials, solid state microelectronics and biotechnology; the Advanced Technology Center of Southeastern Pennsylvania, located at the University City Science Center in Philadelphia, has identified its primary areas of research and development as advanced sensor technologies, human adaptability in space, advanced biomedical technologies, and technology to benefit the handicapped; the Western Pennsylvania Advanced Technology Center, a consortium led by Carnegie-Mellon University and the University of Pittsburgh, has emphasized the area of robotics, high-technology materials, processes and devices including coal technologies, biological/biomedical technology, and metals; the Advanced Technology Center of Central/Northern Pennsylvania, based at the Pennsylvania State University, has targeted electronic materials, food and plant productions/energy conservation, Pennsylvania coal research, biotechnology and manufacturing technologies.

Although the research and development focus of the Ben Franklin Partnership in the areas just described is vitally important, the Ben Franklin Partnership has recognized the essential need for providing support services to entrepreneurs as an integral part of the state's economic development strategy. This assistance helps create and retain jobs. The Small Business Development Center network has been the key to the delivery of such entrepreneurial assistance in the state of Pennsylvania. In the past two years, technology-based companies counseled by the SBDC have been able to create 653 new jobs and retain another 864 jobs.

The SBDC program has demonstrated that true partnerships can be developed with federal and state governments, universities, and the private sector. Although the SBDC's mission is a broad one designed to serve all types of businesses, nearly three-quarters of a million state dollars and approximately an equal amount of federal dollars is being directed at small and medium sized advanced technology companies. The SBDC's efforts have focused on two issues: the formation and growth of technology-based companies and the ability of existing firms to incorporate technological innovations into their operation.

For the 200,000 small businesses in Pennsylvania, as well as for many more medium-sized firms, understanding how changes in technology can improve their productivity will increasingly determine their competitive advantage and employment future.

For some of these firms in-house expertise or private sector vendors will provide the technical knowledge necessary for growth. However, for a much larger number of small and medium-size businesses acquiring knowledge of technological solutions or applications for their products or services is haphazard. Most small businesses cannot employ a large or diverse enough staff to enable them to incorporate and implement technological changes. Many companies are not even aware of new technologies which could be used to increase productivity and/or reduce costs. In addition, it has been well documented that a lack of management expertise is the leading cause of business failure. This holds true for all small companies.

What I have been saying here is that small innovative companies have several problems: their resources to implement new technologies are scarce, their awareness of current technologies is limited, and in almost all situations their business management skills are weak.

In order to help these companies meet the challenge of solving such problems, the PASBDC has incorporated into its basic management assistance a number of specialized activities. For example, the Small Business Development Center at Lehigh University has proposed the creation of a technology-audit process to be applied to small and medium-sized companies. This would enable trained specialists to review a company's production processes and identify areas in which new technologies can be applied. Such an audit program has been operating in other parts of the state with excellent results.

The Office of Small Business Legal Services, a unit of the Wharton SBDC, has provided specific assistance in the areas of initial incorporations and intellectual property protection such as patents, copyrights, and trademarks.

The SBDCs have helped hundreds of advanced technology companies prepare business and financing plans. The results of these efforts can best be demonstrated by example. Let me give you two case histories of businesses which have been assisted in the financing and business planning process.

I will begin with a familiar story -- an inventor has developed a great idea to improve a manufacturing process, but has no time or capital to develop and market the product. Such was the case of Denver X-ray Instruments, Inc., a small company located in the community of Altoona, Pennsylvania and engaged in residual stress measurement. Denver X-ray had developed a technology to alleviate stress testing problems through an innovative technique of bouncing an X-ray beam off an item to two pre-described points. In the developmental process, however, it became clear that this process was time-consuming and not always accurate. It was Dr. Clayton Ruud, an associate professor of engineering science and mechanics at Pennsylvania State University and an officer of Denver X-ray, who perfected the stress measurement process even further by developing a device using fiber optics to catch the reflected x-rays. With this new technology Dr. Ruud was able to perfect a stress analyzer that was more accurate, much faster, much smaller and more portable than any existing units on the market. As is typical of a new inventor, Dr. Ruud did not have the time to develop and market the unit so this was left to the general manager of Denver X-ray. As the company searched for financing, the general manager was advised to contact the Small Business Development Center at St. Francis College to prepare a complete financing proposal package. The first meeting between Denver X-ray and an SBDC consultant took place on June 16, 1986. After several more meetings, a creative financial proposal was developed which used private investor, commercial, and government financing. In July, the company received approval on a commercial loan request for $75,000. In addition the company received another $75,000 from the city of Altoona's Economic Development Loan Fund. The company will also soon be receiving $150,000 from a private investor group that was put together by Altoona Enterprises.

Denver X-ray has recently become the fifth and largest tenant of the Altoona Area Incubator and plans to begin hiring and training employees in the immediate future. Denver X-ray is an excellent example of a company with a great invention but an unclear course of action. Through the cooperative efforts of the company, Altoona Enterprises, and the SBDC, Denver X-ray's future is now developing quite clearly.

The second example is a story of an entrepreneur who saw a need, articulated a solution and, with the help of state university designers, the Ben Franklin Partnership and the SBDC, obtained the financing to develop and manufacture his product.

An engineer who worked for a manufacturer of combustion equipment saw that there was no mechanism to keep furnaces burning at maximum efficiency. He came up with the idea of a computer that could be installed in industrial furnaces to moniter the air/fuel mixture and then sought help to implement his idea. Using his own funds, he had a prototype designed at the electronic engineering and design lab at Penn State University. The next step was to seek the funding necessary to manufacture the prototype. He applied for a grant from the Ben Franklin Partnership, a program that gives grants to emerging technology-based firms with the potential for a rapid increase in sales and significant job creation. To be eligible for such a grant, a firm must present a thorough business plan that includes detailed market and financial information. At this point, the

Ben Franklin Partnership referred the entrepreneur to the SBDC at Penn State. The largest portion of PASBDC consulting time is spent on helping small firms develop the business plans necessary to obtain start-up and growth financing. The SBDC helped him to assemble the financial information he needed to present to the Partnership and the local banks. On the basis of his sound business plan and his good idea, the entrepreneur found a bank willing to provide loans for equipment and working capital and received a 100,000 dollar grant from the Ben Franklin. As the firm has grown, the SBDC has helped him prepare the financial forecasts to get the additional funding he has needed. Still in its very early stages and currently housed in a Harrisburg incubator, the firm now has eight employees and has begun to make a profit. The owner has developed a national distribution network and has begun to export his computers to Canada and Central America.

In addition to helping launch new firms, the SBDCs also consult existing firms in technology issues. Over the years, the Buçknell University SBDC has helped firms that manufacture products as diverse as candles and circuit boards.

It is this latter company which came to the SBDC because it was concerned that the solvent it was using to clean the wires for the circuit boards was toxic. The company had been pouring the used solvent into the sewer and due to the new hazardous waste regulations became concerned with disposing of the solvent in this manner. The company had both electrical and industrial engineers on its staff but did not have anyone with a chemical engineering background. After analysis at the university, it became clear that this was, in fact, a very toxic solvent and after much investigation, the only alternatives presented to the company for disposing of the solvent were extremely costly. The company was purchasing 75 drums a year of solvent and the predicted new costs of disposal were so prohibitive as to cost nearly as much as the initial purchase. The SBDC was able to identify a chemist at the university who developed a still to recycle the solvent rather than dispose of it. Use of the still has resulted in an enormous cost saving to the company which now needs to purchase only 5 drums of solvent a year and has no cost of disposal and no toxic waste.

Seminars and educational programs continue to be an avenue for providing small businesses with the kinds of information on new production processes, innovative technologies and related subjects which enable them to better position themselves in today's competitive markets. Examples of the types of programs the SBDCs have recently offered include "Computer Assisted Measurement and Control: Solution to Applications Problems,"; "Microcomputer Accounting"; "How to Select a Patent Attorney". Several SBDCs have run seminars on the "right to know" laws and how to comply with the new hazardous waste regulations. Nearly 200 people attended such a seminar in Pittsburgh sponsored by Duquesne University. Access to information on this subject will result in tremendous savings to small companies. Another specialized seminar was presented in Philadelphia by the Wharton SBDC and was entitled "Building a Successful Application Software Company." Three hundred people attended a four-week series on this specialized area of technology development.

A role which the SBDCs have successfully played for small companies is that of the "honest broker." Because of their university, non political affiliation, the SBDCs have been able to put together partnerships made up of many diverse participants. A recent initiative undertaken at the Wharton School by the Snider Entrepreneurial Center was a seminar on joint venture strategies. This well-attended, day-long symposium was another approach to improving the competitive posture of Pennsylvania's small companies. Many technology-based firms are stymied when faced with the expense of entering the marketplace with a new product. Often the small companies require the marketing muscle, sophistication, and worldwide credibility of a larger firm to provide the mechanism for entry. Because of this, more and more strategic partnerships have been developed between small and large firms that have provided capacity to the small firms and allowed them to develop worldwide distribution channels. This particular conference provided an opportunity to bring together small companies with large firms and a program which was scheduled to run until 6:30 p.m. ran until after 8:00 p.m. because of the demand of the attendees.

The universities' role in seminars such as these is to provide an access vehicle which allows the transfer of information to take place. It is one more way to help tackle the perpetual problem of the small business owner -- the problem of capacity. I will use an analogy which I have probably used before but if you can picture a small business owner using all ten fingers to plug up the holes in the dike while the water is quickly rising to eyeball level. He must use all his strength to pull himself up to breathe and does not have the additional resources needed to climb over the fence and avoid the oncoming water. Each new problem which a small business owner must deal with on a day-to-day basis is perceived as another enormous hurdle. It is our role to ease the company over these hurdles.

If we believe the data that says small companies are 24 times as effective per research and development dollar as large companies, then we must assume that we're generating a whole lot more innovation in these small firms. We must use that innovation and capitalize on it. We must continue to develop linkages and create opportunities for small companies to work together with large companies, government organizations, universities, and other representatives of the private sector. We must enable small companies to take advantage of money that has already been spent by larger companies, governments, and universities in establishing beachheads. It is the SBDCs role to make that happen, to create new ways for small companies to work efficiently and effectively and allow all of us to use the natural advantages we already have.

Thank you, Mr. Chairman, for the opportunity to present this testimony. I would be happy to answer any questions.

PREPARED STATEMENT OF FRED HALE, STATE DIRECTOR, SMALL BUSINESS DEVELOPMENT CENTER, ST. LOUIS, MO

Small
Business
Development
Centers

I have been asked to present briefly two programs being operated by the Missouri Small Business Development Centers that, in my opinion, can have a positive impact on the ability of small businesses to remain competitive -- even under increasing import pressures.

I think it will be helpful first, however, to introduce the Missouri SBDC. The host organization -- St. Louis University in St. Louis -- contracts with fifteen other institutions of higher education and the Economic Development Department of the State of Missouri to operate eighteen Small Business Development Centers throughout the State. The SBA is our principal Federal sponsor of the SBDC portion of our program.

State Office
(314) 534-7204
St. Louis University
3674 Lindell Boulevard
St. Louis, Missouri 63108

Missouri Technology Development Center

One of our new centers -- The Missouri Technology Development Center (TDC) located at Central Missouri State University in Warrensburg, Missouri -- serves SBDC clients statewide by providing direct assistance in applying technology to solve operational problems facing Missouri businesses.

The Missouri legislature with leadership from then Governor Kit Bond created four state funded Innovation Centers to assist in the development of new "high-tech" companies. As potentially important as these centers are, they missed the mark in addressing the needs of most Missouri firms to become more competitive and efficient by applying existing technology.

The Technology Development Center fills this gap. This program is an applied technology or technology transfer program that assists Missouri firms in moving from "no-tech" to "low-tech" or from "low-tech" to "medium-tech," and in the process, becoming more competitive. Many Missouri businesses -- like their counterparts throughout the Midwest -- are operating in much the same fashion as they have for years in the past. We have seen little or no change in production processes, materials, information systems, product design, and operational systems over the years.

During the same period we have seen an explosive growth in new high technology developments. The problem facing many businessmen and women is not a technology problem -- we have the technology -- the problem is a technology *transfer* problem The typical small business is facing a "*technology application gap* "

Our Technology Development Center assists these business people in understanding and applying existing technology to the operation of their business

For example -- when most small businessmen and women hear the term "robotics" they immediately visualize the multi-million dollar devices used by the big three auto makers and *not* the thousand dollar "pick and place" off-the-shelf device that can, when appropriately applied, economically improve their production efficiency and their comptetitive position

Many machine companies, used to working with metal, find it hard to believe that certain new plastic materials are machinable, stronger, lighter, and maybe, even less expensive than traditional materials

Small businesses are not yet realizing more than a fraction of the efficiencies and competitive advantages offered by specialized and customized applications of personal computers in process and control applications Small business people are still basicly afraid of the computer

The mission of the TDC is to assist Missouri businesses in bridging the "technology application gap " While it is still too early to effectively measure the economic impact of our Technology Development Center, the number of clients and their excitement indicate we are certainly meeting an overwhelming need.

Trade Adjustment Assistance Center

The Missouri SBDC in mid-December, 1986, was awarded the contract to operate the Mid-America Trade Adjustment Assistance Center (TAAC) in the six state region including Missouri, Kansas, Oklahoma, Arkansas, Louisiana, and Texas. This program is funded by the Office of Trade Adjustment Assistance of the International Trade Administration of the U.S. Department of Commerce.

The TAAC program authorized by the Trade Act of 1974 helps producing companies (manufacturers, processors, etc.) adjust to business problems caused by competition from imported products. The Federal Government throughout the thirteen TAAC's across the country pays up to 75 percent of the cost of professional consultants and technical specialists to help certified firms address marketing, engineering, management, production, and similar problems in order to again become competitive.

This program over the years has proven to be a successful approach of assisting businesses combat the competitive pressures of imported products. While not created as "a small business" program, most businesses assisted in the Mid-America TAAC area are small businesses under existing Federal definitions.

The innovative approach I have been asked to mention is not the TAAC program or the SBDC program, but rather the merger of the TAAC program with the Small Business Development Center program to more effectively meet the needs of small business in the region.

The Mid-America TAAC, instead of operating from only one location in the six state region, will use the local Small Business Development Centers in the six states to publicize the program and to identify potentially eligible firms from each local area.

By utilizing the existing SBDC networks in the six states, the Missouri SBDC was able to create an operating network of more than 50 locations to reach eligible firms. Since all locations were already in operation; well known in their communities; and quite knowledgeable about characteristics and capabilities of local firms, the scope and impact of the TAAC has been greatly enhanced.

Additionally, the capabilities of both the TAAC and the SBDC now available through the same network allows efficient delivery of the most comprehensive collection of services available to help small businesses in the six states regain a competitive advantage.

Training is presently underway within the SBDC network to equip local SBDC personnel throughout the region with the knowledge and tools to effectively carry the TAAC message and to identify potential forms to be certified for TAAC support.

The St. Louis University School of Business and its Missouri SBDC is proud to have a lead role in coordinating the activities of two successful Federally sponsored business assistance programs (TAAC and SBDC) under a single efficient system to deliver more direct help to more small business spread more evenly through the six state region than ever before.

Conclusion

I would hope your committee as it explores ways to help small businesses regain their competitive edge, will consider the importance of technology transfer and of centers like the Missouri Technology Development Center to assist small businesses take advantage thereof.

I would also hope that the efficiencies we have demonstrated by combining the administration of multiple programs through a single delivery system might prove useful in the committee's deliberations.

Thank you for the opportunity to share these thoughts with you.

PREPARED STATEMENT OF MARY A. WATHEN, PRESIDENT, KOBOWAY, INC., COSTA MESA, CA, AND REPRESENTING THE AMERICAN ELECTRONICS ASSOCIATION

Mr. Chairman, my name is Mary A. Wathen, and I am President of Koboway, Inc. of Costa Mesa, California. Koboway is a small business that employs 145 people in the manufacture of printed electronic circuit boards. In the last two years, the number of circuit board manufacturers in the United States has diminished from about 1000 to 600 due to many companies moving their operations off-shore. There are a variety of reasons why firms off-shore. Many are directly related to the tax, trade, and regulatory environment here in the U.S. I'll discuss some of these issues in greater detail in my testimony.

I am here today representing the American Electronics Association, which is the nation's largest high technology trade association consisting of 3,250 companies across America. AEA membership is representative of all segments of the industry, including computers and computer components, semiconductors, instruments, telecommunications, and software. Three-fourths of AEA's members employ fewer than 250 people. The work of the House Small Business Committee is therefore of interest to AEA's membership.

Mr. Chairman, on behalf of AEA I want to thank you for offering the association an opportunity to appear before the committee.

THE ELECTRONICS INDUSTRY IS THE LARGEST MANUFACTURING EMPLOYER I THE U.S.

Electronics is a vital segment of the American economy and a toolmaker that enables other industries to strengthen productivity and competitiveness. Between 1978 and 1984, the electronics industry created over a million new jobs in the U.S. Electronics now directly employs 2.5 million Americans and may indirectly in related industries.. The chart on the last page shows that the industry employs four times more people than either motor vehicles or aerospace and six times more than steel We in the electronics industry are very proud of this contribution. We believe that it reflects the traditional preeminence of our technological innovation as well as the stron competitive posture of our industry.

There is evidence, however, that this strong competitive position is eroding. The United States' world-wide trade in electronics products has fallen from a surplus of $7.4 billion in 1980 to a deficit of $13.1 billion in 1986. Employment in the industry has remained flat since 1984.

My testimony today will address four issues now before Congress that impact the electronics industry. These issues are: trade, tax policy, procurement policy, and occupational safety.

TRADE POLICY: INCREASE EXPORTS RATHER THAN LIMIT IMPORTS
The electronics industry does not look to Congress to legislate the trade deficit away. Rather, we believe it is the responsibility of industry to compete more effectively. However, the U.S. government shapes the international economic environment in which we do business. In particular, we in industry must rely on the U.S. government to eliminate overseas barriers which restrict our access to foreign markets as well as unfair advantages which our competitors receive from their own

governments.

AEA opposes the imposition of import barriers such as tariffs and quotas for the purpose of protecting any American industry. In our view, such barriers represent a surrender to foreign competition and an admission that the U.S. is second best.

Tariffs only address imports, and I will remind the committee that as a fraction of Gross National Product (GNP) imports of manufactured goods are today less than their level in 1980. However, exports have fallen even faster. Therefore, remedies to the trade imbalance should focus on promoting exports rather than limiting imports.

Trade Law reform

AEA believes that trade law reform should be designed to increase the access of U.S. companies to overseas markets. To help achieve this objective AEA supports launching a new round of multilateral trade negotiations, as well as the aggressive enforcement by the Government of U.S. rights against foreign unfair trading practices.

To accomplish these objectives, we believe Congress should approve authority for a new round of multilateral trade negotiations. These negotiations should be designed to develop new international discipline in the areas of intellectual property protection, trade-related investment distortions, and services such as data processing. The negotiations should also extend current international discipline in such areas as government procurement.

In addition to extending current international rules, we believe it is critical that the Executive Branch enforce both the letter and spirit of current agreements. To accomplish this, we believe that as a last resort the U.S. should be prepared to limit foreign access to the U.S. market as leverage to enforce compliance with agreements and legitimate U.S. rights.

Two pertinent examples of attempts to enforce the rights of U.S. electronics companies are Section 301 cases against Japan in semiconductor trade and Brazil for its informatics policies. In both of these cases, U.S. trade officials have been seeking to eliminate practices which unfairly restrict competitive opportunities for U.S. electronics companies. As yet, neither effort has been completely successful, but we are encouraged by the aggressiveness with which our negotiators have sought solutions to these problems.

In order to sustain this effort on behalf of U.S. commercial interests, AEA supports strengthening in the trade bill the tools available to U.S. trade officials to work toward these objectives. AEA opposes automatic retaliation against trading partners except in those limited cases where there has been a positive GATT finding that a foreign practice is in violation of international trade rules. In particular, AEA believes the amendment proposed to H.R. 3 by Chairmen Rostenkowski and Gibbons is a step in the right direction.

National Security Export Controls

In addition to these measures, unnecessary disincentives to exports must be removed. In particular, national security export controls, which are required to prevent the Soviet Bloc from acquiring U.S. technology, are administered in a way that places U.S. firms at a disadvantage in competing in Western markets.

A study recently completed by a panel of the National Academy of Sciences found that export controls cost the U.S. $9.3 billion in exports each year and 100,000 jobs. In particular, the study found that it takes small businesses 14% longer than larger firms to receive permission from Washington to export.

AEA supports the proposals that Congressman Don Bonker made in the Foreign Affairs Committee to streamline the export control system in a way that enhances both national security and the ability of U.S. high technology firms to export. The Bonker approach recognizes that it is meaningless to control the exports of goods that are freely available world-wide including to the Soviet Bloc. The Bonker provisions require that export controls be imposed only on those items not now available to the East from other sources.

TAX POLICY: RAISING TAX RATES WOULD HURT SMALL BUSINESSES, BUT TECHNICAL CORRECTIONS TO THE 1986 ACT WILL HELP

One of the most important reasons that AEA and other business groups supported the 1986 Tax Reform Act was its provision to reduce the basic corporate rate from 46 to 34 percent on July 1, 1987. During the 1987 tax year, blended tax rates are in effect and vary according to a company's fiscal year. Among the proposals to reduce the budget deficit is a suggestion by House Speaker Jim Wright to renege on that promise and freeze tax rates at today's rates. AEA opposes efforts to change the scheduled rate reductions. Higher rates simply mean a lower after tax return on increased profits and less money available to grow. In addition, changes in the rate schedule would further complicate businesses decisions that have already been made as a result of the sweeping changes in the 1986 Act.

Some of the provisions of the 1986 Tax Reform Act present a set of special problems for small businesses still in the start-up stage--that phase of the business beginning with substantial capital investment in research and development of product and ending after product is being shipped and income being returned to the company. During this period and during the time when the company begins to return a profit, a typical start-up company passes through difficult financial straits made tougher by the interaction of a number of very technical provisions of the tax code designed to prevent tax abuses.

Working through our unique grassroots structure, AEA has identified several technical problems deriving from the personal holding company rules, amortization requirements of start-up costs, including R&D expenses, and other treatment of operating losses when a company seeks outside financing.

Corrective action can be taken, we believe, with very little revenue impact. But the results will be important for dynamic entrepreneurial companies. And, the critical transition from concept to reality in the marketplace will be a bit smoother for American companies seeking to development and market American ideas.

AEA is presently developing specific proposals to:

Simplify Amortization of Start-up Costs

The technical rules allowing the amortization of start-up costs should be simplified by eliminating the election requirement, which is a trap for the unwary. If necessary, the few small businesses that may not want to amortize start-up expenditures could be required to make an election not to amortize their expenses.

Limit Reduction of Net Operating Loss Carryovers

The new net operating loss rules operate unfairly to reduce the net operating losses that may be carried forward by start-up companies. This occurs because start-up companies, in the ordinary course of their development, must seek new sources of financing. Common forms of private and public offerings result under the new rules in an "ownership change" that reduces net operating loss carryovers. The rules should be changed to avoid that result in the case of ownership changes caused by private and public offerings of start-up companies that continue their same business.

Improve Small Business Stock Provision

Present law permits individuals to treat losses on certain small business stock as ordinary losses, rather than capital losses. To encourage both individuals and corporations to invest in start-up companies, this provision should also apply to corporations that acquire stock in small business companies.

Research and Development Credit for Start-Up

The research credit rules should be improved to ensure start-up companies qualify their research expenditures for the credit. The incremental research credit only applies to qualifying research expenses incurred in connection with an existing trade or business. If a start-up company has not yet begun selling its products, then, under the pre-operating expense doctrine developed by the courts, its research expenses have not been incurred in connection with an existing trade or business. Accordingly, even though research expenses are deductible, they are not eligible for the credit. As the credit is designed to encourage research in the United States, this restriction seems contrary to its legislative purpose.

The reason for the restriction arises from a desire to prevent individual investors in research and development partnerships from claiming the credit against taxes attributable to investment and other income. However, that purpose could be accomplished by

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coupling the restriction on the credit with the new passive loss rules. Start-up high technology companies should be entitled to a credit for their research activities. If necessary, the credit could be restricted to the tax attributable to business income (as opposed to investment) income.

PROCUREMENT POLICY: REGULATORY IMPEDIMENTS LIMIT THE ABILITY OF SMALL BUSINESS TO CONTRIBUTE TO A STRONG NATIONAL DEFENSE

In recent years, Congress has enacted several procurement reform provisions aimed at ensuring that taxpayers receive value for their dollars. While well-intended, these measures have made it unnecessarily difficult for small companies to conduct business with the federal government, particularly the Department of Defense.

Acquisition of Commercial Products

A top priority fc AEA in 1987 is to implement the statutory preference for nondevelopmental items (commercial products) enacted in 1986 as section 907 of the Defense Authorization Act. AEA is a co-founder of COMPACT, a coalition of industry associations and companies interested in selling commercial items to DoD to replace identical or similar items manufactured according to detailed military specifications. COMPACT has undertaken a major study of contract clause impediments to commercial product acquisition. The researcher will interview contracting officers and identify specific contract clauses routinely required which impede vendors in selling commercial products to DoD.

Deregulation of Federal Contract Procures

AEA's Government Procurement Committee has endorsed a program to reduce unnecessary oversight and regulation of the procurement process. In a free enterprise, market-driven economy, such as ours, the operation of the market does provide checks and balances on common abuses by both government and contractors. For example, if government feels profits earned on a contract are excessive, competition can cure the defect because a hungry vendor will seek to underbid others. On the other hand, if contractors are not earning sufficient profit, the government will find few or no takers on its bid requests.

Small businesses, in particular, cannot afford the extremely high cost of complying with myriad contracting requirements suitable for sole-source, negotiated contracts. We seek to encourage the government, especially the Department of Defense, to do as much business as possible with vendors on terms closer to standard commercial practice. The AEA Government Procurement Committee is collecting data and examples to support legislative and regulatory changes to achieve this goal.

Runaway Audit Policy

The AEA Government Procurement Committee is now studying the problems and costs created by duplicative, and unnecessary audits. The objective is to build a credible, accurate analysis of the types of audits being conducted by DoD and the costs sustained by contractors undergoing such audits. An example involves an AEA member company which underwent 123 separate audits in which only a small dollar amount in mischarges were uncovered on more than $23 million of business.

OCCUPATIONAL SAFETY: NECESSARY IN THE WORK PLACE BUT WITHOUT NEW ADMINISTRATIVE BURDENS

In the environmental and occupational health fields, AEA small member companies share with their large company counterparts a commitment to effective compliance with programs aimed at protecting natural resources and our own most valuable resources, our work force.

But small companies share too in a phenomenon that broadly and increasingly characterizes our efforts to manage environmental resources and protect our employees. I am speaking here not necessarily to the stringency of the regulatory programs, but rather to the frequently bewildering complexity of them.

The electronics industry--both its large and small company members--is recognized throughout the country as respecting and complying with stringent scientifically-based standards for environmental protection and industrial hygiene. Indeed, our industry's unique needs for manufacturing purity and cleanliness demand no less, and the same is true of our highly skilled and highly educated--and therefore highly valuable--work force.

It often is not the stringency of sound environmental policies that frustrate small businesses as much as it is the extraordinary volume, complexity, internal contradictions, and administrative and paperwork burdens frequently characterizing those programs.

Each year, the Environmental Protection Agency, the nation's single largest regulatory agency, commands a lion's share of the pages published in the Federal Register. The volumes the agency produces--frequently detailing highly complex and arcane issues in language best suited for a post-doctoral dissertation--provide a daunting challenge to the largest of companies, let alone the smaller companies wanting to comply with both the spirit and the letter of the law, but also with limited technical resources.

Examples abound. But two very current examples will illustrate the situation.

Superfund

The 1986 Amendments to the Superfund law establish in Title III a completely new program requiring that facilities using, manufacturing, or storing a wide range of chemicals report the presence and quantities of those chemicals to the surrounding community. What is especially important here is that we limit those threshold reporting quantities to limits which indeed can pose a potential public health risk. It would indeed be foolish if, as has been proposed, we were to set a threshold reporting quantity of "zero", in which case voluminous reports concerning laboratory-scale chemicals and high school chemistry classes would be inundating local governments and agencies with numerous reports in what could only be considered regulatory overkill. Effective congressional oversight of this sweeping new community right to know program--specifically as it may affect small businesses--can help to mitigate the negative impacts the program could have on small business.

Worker Notification

Another example of the need to be cognizant of the impacts on small businesses lies in the worker notification legislation now before the House of Representatives. H.R. 162 would mandate that employees would be officially notified by a newly established Risk Assessment Board if they are judged by that board to be "at risk" of an occupational illness or disease resulting from a work place exposure to a hazard.

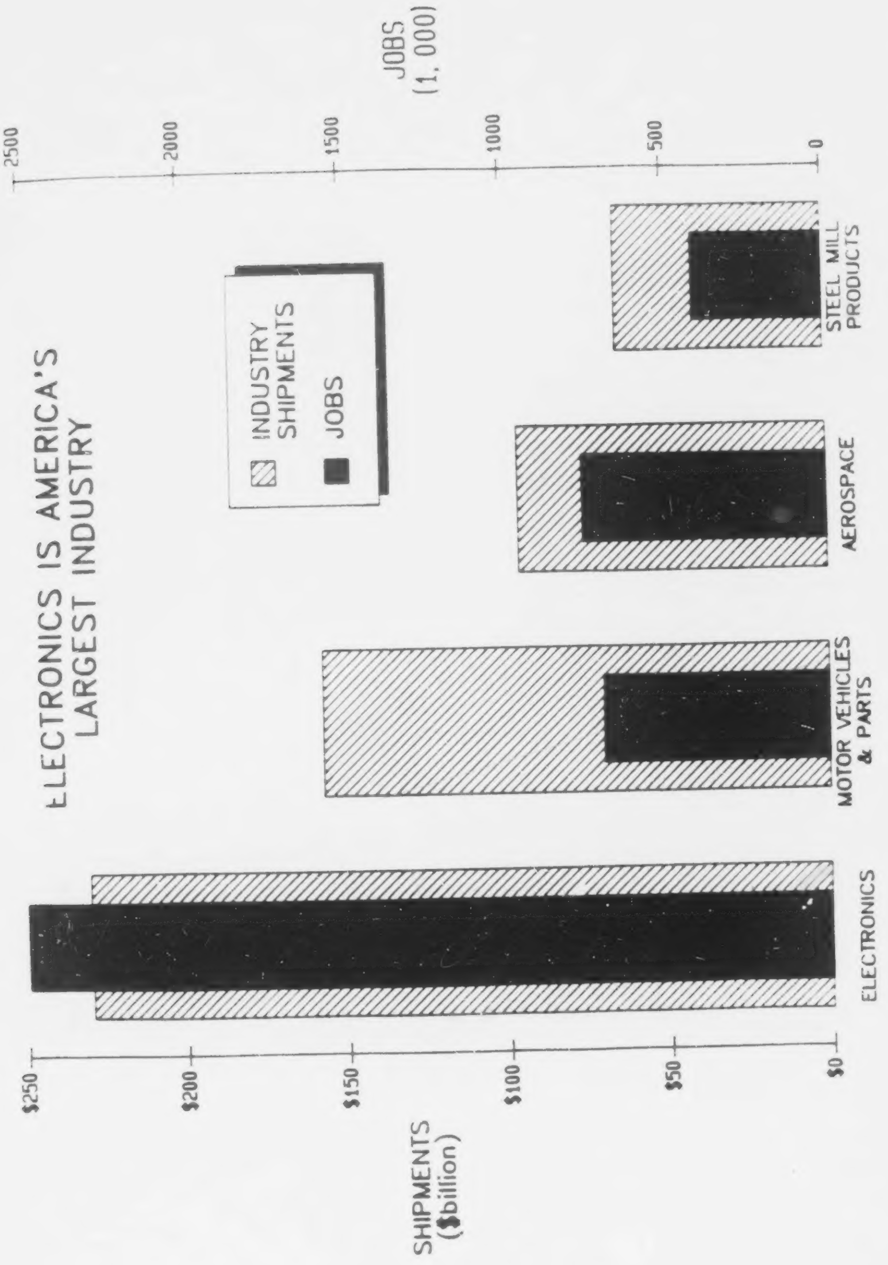
It is essential, in any legislation, that notifications be targeted to only those worker populations which sound scientific principles show to be at possible risk of an occupationally-related illness or disease. It is critical also that all employers'--especially small employers'--liabilities be appropriately protected against unwarranted individual claims resulting from a notification which is, at best, aimed just at broad populations, and not at specific individuals.

Given the enormous challenges facing small business in the face of globally competition, it is crucial that legislators, in evaluating proposals such as H.R. 162, be mindful of the potentially catastrophic impacts on small businesses.

CONCLUSION

In summary, Mr. Chairman, there are several competitive obstacles that now face small high technology companies. I've mentioned the key issues in my testimony that face AEA members. Although other committees in the House have primary jurisdiction over some of these issues, I hope that committee members will add their voices in the House for the electronics industry and advocate changes that will help improve the economic environment in which we compete.

Thank you for the opportunity to present this testimony today. I would be glad to answer any questions.



ELECTRONICS IS AMERICA'S LARGEST INDUSTRY